STATEMENT 3: FISCAL STRATEGY AND OUTLOOK

The Government has set a pathway to return the budget to balance in 2015-16 and to surplus by 2016-17, improve the sustainability of Australia's public finances and build on Australia's record of fiscal and economic strength.

While Australia's economic fundamentals remain strong, tax receipts have been significantly affected by weaker than expected nominal GDP growth. The widespread effect of the persistently high Australian dollar on profits, combined with the impact of falling commodity prices, has resulted in lower than expected corporate profitability, and thus lower company tax receipts. A slower recovery in capital gains tax and lower than expected resource rent taxes have compounded the fall in company tax receipts over the forward estimates.

A more gradual return to surplus is appropriate given significant downgrades to revenue and the transition underway in the economy towards new sources of growth. Attempting to return to surplus too quickly by making drastic cuts in the near term would come at a significant cost to jobs and growth.

The Government continues to deliver on its commitment to the medium-term fiscal strategy by choosing a sensible pace of consolidation, which strengthens Australia's public finances, on a timetable consistent with maintaining solid growth and low unemployment.

The Government has offset all new spending decisions since the 2009-10 Budget. There is $43 billion in responsible savings in this Budget, building to a total of over $180 billion of savings in the six budgets since 2008-09. Long-term savings will continue to benefit the budget beyond the forward estimates.

The Government is continuing to build a stronger economy, a smarter nation and a fairer society through key productivity enhancing investment, such as the National Plan for School Improvement, *DisabilityCare Australia*, and critical infrastructure. These investments are fully and sustainably funded over the medium term.

This Budget provides a clear plan for moving the underlying cash balance from a deficit of $18.0 billion (1.1 per cent of GDP) in 2013-14, into balance in 2015-16 and a surplus of $6.6 billion (0.4 per cent of GDP) in 2016-17. All spending decisions across the forward estimates are fully offset by savings. Policy decisions made in this Budget will deliver the largest improvement to the forward estimates position in nearly two decades.

Australia's financial position remains amongst the strongest in the developed world. Net debt is expected to peak in 2014-15 and come down after that. Australia's net debt as a share of GDP is expected to peak at less than one-eighth of the level in the major advanced economies.

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STATEMENT 3: FISCAL STRATEGY AND OUTLOOK

OVERVIEW OF FISCAL POSITION

This Budget strikes the right balance between maintaining a strong fiscal position, supporting economic growth and jobs, and investing in the future.

Responsible saving decisions make room for historic investment in Australian schooling, productivity enhancing nationally significant infrastructure, and ensuring a fairer go for Australians with disability.

The Government has maintained its commitment to its medium-term fiscal strategy with a clear plan to return the budget to balance in 2015-16 and to surplus in 2016-17.

Consistent with this fiscal strategy, the Government continues to deliver fiscal outcomes that have supported Australia's solid growth and low unemployment. A well-designed stimulus package kept the Australian economy out of recession during the global financial crisis. The Government has since delivered a sensible consolidation to ensure Australia's public finances remain strong and that solid growth and low unemployment are maintained.

The Australian economy is expected to undergo two large and important transitions over the forecast period. Following the largest investment boom in Australia's history, the resources sector will transition from the investment phase toward exceptional growth in production and exports. More broadly, the Australian economy will transition to non-resource drivers of growth.

While Australia's economic fundamentals remain strong, the current unusual and persistent combination of a sustained high dollar and falling commodity prices is having a significant and widespread impact on corporate profitability, with the National Accounts measure of company profits falling for a record five consecutive quarters.

Tax receipts have been significantly affected by weaker than expected nominal GDP growth. Weaker commodity prices and the persistently high Australian dollar have hit company profits across most of the economy, including the resources sector. This has had a large impact on the level of company tax receipts expected in 2012-13 and over the forward estimates. Lower than expected capital gains tax and resource rent taxes have compounded the fall in company tax receipts. Since the 2012-13 Budget, tax receipts have been revised down by around $17 billion in 2012-13, bringing the total write-downs in tax receipts over the five years since the 2008-09 Budget to around $170 billion. Since the 2012-13 MYEFO, tax receipts have been revised down by around $60 billion over the four years to 2015-16.

Responding to changing economic and fiscal circumstances is a central element of the Government's fiscal strategy. The Government has chosen to recalibrate the pace of fiscal consolidation to ensure that it does not weaken economic growth in the near term. A more gradual return to surplus is appropriate given the significant downgrades to revenue and the transition underway in the economy. The consolidation is responsibly paced, amounting to around half of a percentage point of GDP a year, on average, from 2013-14 to the end of the forward estimates.

The Government's approach is to let the automatic stabilisers on the revenue side of the budget operate in the near term. This means not offsetting substantial near term revenue downgrades by making large spending cuts, which would come at a significant cost to jobs and growth.

The Government continues to exercise spending restraint, in a way that does not put Australia's solid growth and low unemployment at risk by making drastic cuts in the near term to offset lower than expected tax receipts. The expected overall impact of the Government's policy decisions on economic growth and employment in 2012-13 and 2013-14 is largely unchanged since MYEFO.

Without the net impact of policy decisions in this Budget, there would have been underlying cash deficits of $17.8 billion in 2013-14, $17.4 billion in 2014-15, $11.6 billion in 2015-16 and $5.6 billion in 2016-17.

This Government is taking a measured pathway back to surplus within the forward estimates. Decisions taken this Budget will result in $43 billion of total savings. The net budget impact of policy decisions is a $28.4 billion improvement to the underlying cash balance over forward estimates, including an improvement of $12.2 billion in 2016-17, bringing the budget back to balance by 2015-16 and into surplus in 2016-17, well ahead of most advanced economies.

Table 1: Budget aggregates

	Actual	Estimates			Projections	
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
Underlying cash balance ($b)(a)	**-43.4**	**-19.4**	**-18.0**	**-10.9**	**0.8**	**6.6**
Per cent of GDP	-2.9	-1.3	-1.1	-0.6	0.0	0.4
Fiscal balance ($b)	**-44.5**	**-20.3**	**-13.5**	**-6.3**	**6.0**	**10.8**
Per cent of GDP	-3.0	-1.3	-0.8	-0.4	0.3	0.6

(a) Excludes net Future Fund earnings.

While the return to surplus is more gradual, the Government's fiscal consolidation provides ongoing scope for monetary policy to respond to economic developments as needed. Just as the Government's fiscal settings are consistent with solid growth and low unemployment, they are also consistent with contained inflation. The Government's fiscal consolidation has already given the RBA scope to ease monetary policy, with policy interest rates reduced by 200 basis points since late 2011.

Lower interest rates are already providing support to many sectors, assisting the transition towards non-resource drivers of growth over the forecast period.

Fiscal sustainability is also being improved by implementing policies that increase long-term growth in the economy, and boost Australia's productivity through investment in education, skills and critical infrastructure.

The Government's commitment to fiscal restraint will ensure that Australia's fiscal position remains one of the strongest in the developed world.

By the time Australia is expected to return the budget to balance in 2015-16, the IMF estimates that 24 out of 35 advanced economies will still be in deficit.

Net debt is expected to peak at 11.4 per cent of GDP in 2014-15, reducing to zero by 2021-22. While average net debt for the major advanced economies is expected to peak at 92.6 per cent of GDP in 2014, Australia's net debt as a share of GDP is expected to peak at less than one-eighth of that level.

The Government's fiscal strategy

Within the framework of the Government's medium-term fiscal strategy, Australia's fiscal policy settings have helped the Australian economy remain resilient through the global financial crisis and severe global economic turbulence in recent years.

The fiscal strategy is designed to ensure fiscal sustainability over the medium term, but it also provides the necessary flexibility for the budget to vary in line with economic conditions in the short term to support macroeconomic stability.

Adhering to the fiscal strategy will allow the economy to continue to remain responsive to global challenges and the effect they have on our economy, while reducing net debt over time and keeping government borrowing costs low.

The medium-term fiscal strategy has remained unchanged since 2008-09, the Government's first budget (see Box 1 below).

Box 1: The medium-term fiscal strategy

The Government's medium-term fiscal strategy is to:

- achieve budget surpluses, on average, over the medium term;
- keep taxation as a share of GDP, on average, below the level for 2007-08 (23.7 per cent); and
- improve the Government's net financial worth over the medium term.

To ensure a timely return to surplus and recovery in the fiscal position, since the beginning of the global financial crisis the Government has further committed to:

- allow the level of tax receipts to recover naturally as the economy improves, while maintaining the Government's commitment to keep taxation as a share of GDP below the 2007-08 level on average; and
- build growing surpluses by holding real growth in spending to 2 per cent a year, on average, until the budget surplus is at least 1 per cent of GDP, and while the economy is growing at or above trend.

This Budget provides a pathway to budget balance in 2015-16 and increasing surpluses from 2016-17, which will improve the Government's net financial worth over the medium term. Real growth in spending has remained low, at an average rate of 1.3 per cent from 2012-13 to 2016-17, the lowest five-year average growth rate for 25 years.

Taxation as a share of GDP over the forward estimates is expected to average 22.5 per cent, which is 1.5 percentage points lower than during the last four years of the previous government.

Estimates of taxation receipts have declined significantly

The Australian economy continues to outperform most of the developed world. Australia's level of real GDP is significantly above its pre-global financial crisis level, in stark contrast to the major advanced economies. Australia's real GDP is also expected to continue to grow faster than most of the developed world over the forecast period, building on Australia's impressive record of economic growth and job creation over the past five years.

Nevertheless, it is nominal as opposed to real GDP that ultimately determines government revenue and the Government's fiscal position, and over the year to December, nominal GDP grew by only 2.0 per cent, well below real GDP growth of 3.1 per cent. Nominal GDP reflects both production and prices for Australian output.

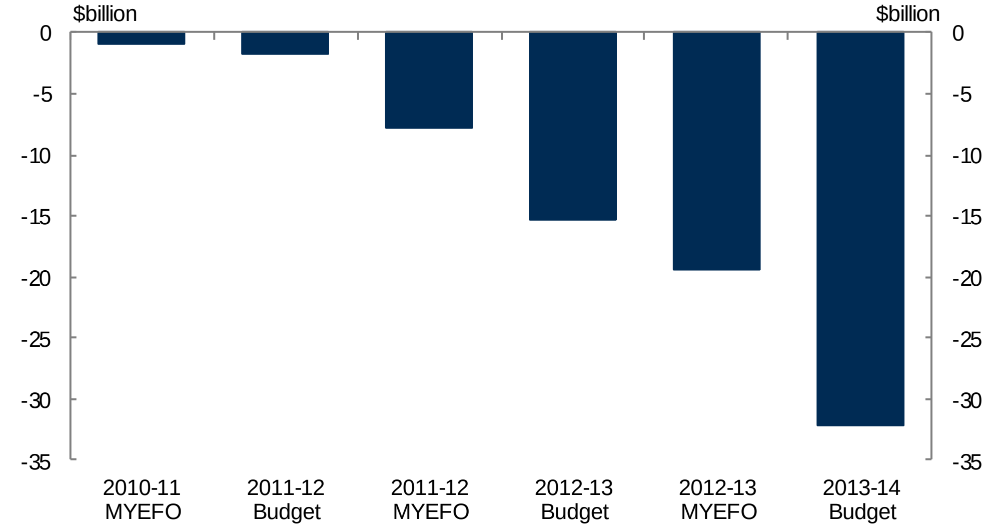
The unusual combination of a persistently high dollar and falling commodity prices is having an acute and persistent impact on prices and profitability across the economy, including in the resources sector. Consumer caution and changing spending patterns have added further competitive pressure on retailers. Firms have been absorbing costs rather than passing them on as higher prices, which has reduced profit margins.

Tax receipts have been significantly affected by these changes. Lower company profits across most of the economy have had a significant impact on the level of company tax receipts expected in 2012-13 and over the forward estimates. Lower than expected capital gains tax (CGT) and resource rent taxes have compounded the fall in company tax receipts. Income tax withholding and consumption taxes have been revised down to a lesser extent, as wages are expected to grow modestly and consumption is expected to remain solid over the forward estimates.

Since MYEFO, tax receipts have been revised down by $12.9 billion in 2012-13 and $16.6 billion in 2013-14. Company tax receipts have been revised down by around $5.2 billion in 2012-13 and $7.2 billion in 2013-14. CGT, an important component of individuals, companies and superannuation funds tax, is also contributing to the weaker revenue outlook. Since the 2012-13 MYEFO, total CGT receipts have been revised down by $1.8 billion in 2012-13 and $2.9 billion in 2013-14. Resource rent taxes have been revised down by $3.6 billion in 2012-13 and $3.2 billion in 2013-14.

Tax receipts have been revised down by around $170 billion over the five years to 2012-13. For 2012-13 alone, tax receipts (excluding policy decisions) have been revised down by around $32 billion since the 2010-11 Budget (see Chart 1 below).

Chart 1: Cumulative tax receipts write-down in 2012-13 since the 2010-11 Budget



Source: Treasury.

Across the forward estimates, tax receipts as a share of GDP are expected to remain well below pre-global financial crisis levels. The tax-to-GDP ratio in 2013–14 is estimated to be 22.2 per cent, 1.8 percentage points lower than the average of the five years prior to the global financial crisis of 24.0 per cent.

These revenue write-downs have made fiscal consolidation more challenging, with larger policy adjustments needed to achieve the same budget outcome. The Government continues to exercise spending restraint, but will not put Australia's solid growth and low unemployment at risk by offsetting substantial revenue write-downs in the near term.

Maintaining fiscal discipline has kept the budget on a pathway to surplus

It is important that the pace of fiscal consolidation is calibrated to economic circumstances to avoid a detrimental impact on growth and jobs.

A measured pathway back to surplus is in line with principles of sound economic policy, striking the right balance between protecting Australia's solid growth and low unemployment, maintaining a strong fiscal position and improving fiscal sustainability in the medium term.

The IMF has said in its April 2013 *World Economic Outlook* that 'in advanced economies, the right macroeconomic approach continues to be gradual but sustained fiscal adjustment, built on measures that limit damage to activity'.

In Australia, revenue write-downs have considerably increased the fiscal adjustment needed to return to surplus, relative to expectations at the time of the 2010-11 Budget when a surplus in 2012-13 was initially forecast. Budget Statement 4, *Fiscal Policy in the Current Economic Environment,* shows that at the time of the 2010-11 Budget, returning to surplus in 2012-13 required a fiscal adjustment, over and above the automatic impacts of the economic cycle and unwinding of the temporary stimulus, of around 1.6 per cent of GDP.

Cumulative parameter variations since the 2010-11 Budget have increased the required fiscal adjustment to 3.4 per cent of GDP; more than double the originally anticipated adjustment.

Offsetting the significant revenue write-downs since MYEFO in such a short timeframe would have come at a significant cost to jobs and growth. This would lead, in turn, to even lower revenue and increased spending on unemployment benefits.

Given this, the timing of the consolidation has been recalibrated to manage its impact on growth and jobs. Since the global financial crisis, the temporary stimulus measures have been withdrawn and spending discipline imposed, with the fiscal consolidation between 2011-12 and 2012-13 alone equivalent to 1.6 per cent of GDP.

The change in the pace of consolidation over the forward estimates is largely owing to the significant write-down in tax receipts.

From 2014-15, policy decisions are expected to have a more significant role in the fiscal consolidation than in 2013-14. All new payment decisions within the forward estimates have been more than offset by payments savings measures.

Savings

Fiscal discipline involves ensuring that any expansions in one area are matched by responsible savings in other areas, in addition to any savings needed to continue fiscal consolidation in support of the Government's medium-term fiscal strategy.

All new decisions taken in this Budget have been more than fully offset, contributing to the return to surplus.

Table 2 shows the effect of spending and savings decisions since MYEFO. The net budget impact of policy decisions takes into account amounts that were previously provisioned for in the Contingency Reserve (and as a result have no net impact on the budget position). These principally relate to the continuation of the Early Childhood Education National Partnership, and Official Development Assistance.

Table 2: Effect of spending and savings decisions in the 2013-14 Budget[(a)]

	Estimates			Projections		
	2012-13	2013-14	2014-15	2015-16	2016-17	Total
	$m	$m	$m	$m	$m	$m
Effect of policy decisions since MYEFO						
Spends	**-2,604**	**-2,470**	**-3,212**	**-2,853**	**-4,465**	**-15,604**
Payments	*-2,474*	*-2,386*	*-3,172*	*-2,857*	*-4,437*	*-15,325*
Receipts	*-130*	*-83*	*-41*	*4*	*-28*	*-278*
Saves	**246**	**1,750**	**9,400**	**15,176**	**16,471**	**43,043**
Payments	*172*	*1,411*	*3,756*	*5,660*	*6,295*	*17,294*
Receipts	*75*	*338*	*5,644*	*9,517*	*10,175*	*25,749*
Total effect of policy decisions since MYEFO	**-2,358**	**-720**	**6,188**	**12,324**	**12,005**	**27,439**
Add Contingency Reserve offsets to policy decisions	4	433	289	77	195	998
Net budget impact of policy decisions	**-2,354**	**-286**	**6,476**	**12,401**	**12,200**	**28,437**

(a) On an underlying cash basis.

The net budget impact of policy decisions is a $28.4 billion improvement to the underlying cash balance over the forward estimates.

The Government has made $43.0 billion in savings in this Budget to pay for new spending of $15.6 billion (of which $1.0 billion had been provisioned for in the Contingency Reserve).

The savings in this Budget build on the $16.4 billion of savings in the 2012-13 MYEFO and more than $130 billion of savings identified in the five budgets since 2008-09. Policy decisions made in this Budget will deliver the largest improvement to the forward estimates position in nearly two decades.

The revenue position has been enhanced by a range of measures, including increasing the Medicare levy to help fund *DisabilityCare Australia*, a package of measures to protect the corporate tax base, and measures to improve the sustainability of the superannuation system. Collectively, policy measures add $25.5 billion to receipts over the five years to 2016-17.

The sustainability of Government finances has also been improved over the medium term as many of the budget savings identified will deliver continuing benefits to the bottom line beyond the forward estimates.

Long-term savings

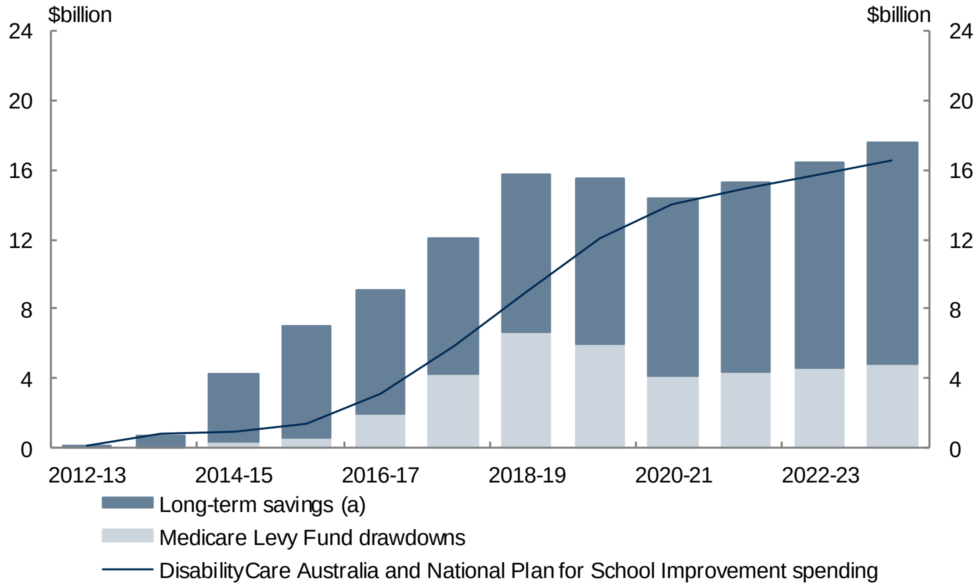
Since its first Budget in 2008-09, the Government has consistently made savings decisions that continue to benefit the budget position beyond the forward estimates.

Significant long-term savings in this Budget include reforms to superannuation and business taxation, the increase in the Medicare levy and reforms to family payments.

These savings build on earlier long-term savings such as means testing the private health insurance rebate, reforming a number of fringe benefits tax concessions and reducing superannuation concessions for very high income earners.

These measures have allowed the Government to fund new priorities such as establishing *DisabilityCare Australia* and the National Plan for School Improvement (Chart 2 below). The enduring savings have also helped improve the budget bottom line, helping to achieve the goals of the Government's medium-term fiscal strategy.

Chart 2: Making room for the National Plan for School Improvement and *DisabilityCare Australia*



(a) Long-term savings from 2013-14 Budget and 2012-13 MYEFO, excluding Medicare Levy and net of Dental Care Reform expenditure.

Without the long-term savings made since the 2008-09 Budget, the outlook would be much poorer (see Box 3 in Statement 4, *Fiscal Policy in the Current Economic Environment*). The long-term savings the Government has made in this Budget and previously mean that the budget is cumulatively better off by over $300 billion by 2020-21. These savings also help to deal with the longer-term budget pressures that were identified in the *Intergenerational Report 2010*. This report showed that without changes to future policy the expenditure pressures from ageing and other factors would create a significant fiscal gap by 2050. Changes to health expenditure, including measures to improve sustainability in this Budget, have helped to reduce one of the most significant contributors to the projected fiscal gap.

Payments

A continuing focus on restraining growth in payments remains an important element of the Government's fiscal strategy. Given the range of factors that can affect payments in any one year, looking at payments over a number of years is a better indicator of spending patterns.

The discipline imposed on real spending growth has kept payments as a share of GDP at or below 24.5 per cent across the forward estimates, dropping to 24 per cent or below by 2015-16. This discipline has also meant that the average payment to GDP ratio over the five years from 2012-13 is lower than the average payment to GDP ratio over the previous thirty years.

Assessing payments over a number of years to judge spending restraint is reflected in the Government's commitment to holding real growth in spending to 2 per cent a year, on average, until the budget surplus is at least 1 per cent of GDP, and while the economy is growing at or above trend.

Table 3: Real growth in payments

	2012-13	2013-14	2014-15	2015-16	2016-17
Real payment growth	-3.2	4.3	2.2	1.4	1.9
Average real growth in payments			1.3		

Table 3 shows that real growth in payments is estimated to be -3.2 per cent in 2012-13, rising to 4.3 per cent in 2013-14 and averaging 1.3 per cent over the five years to 2016-17.

The proportion of payments to GDP decreases over the forward estimates; with all new payments more than offset by reductions in lower priority existing payments.

FISCAL OUTLOOK

Table 4 shows that an underlying cash deficit of $18.0 billion (1.1 per cent of GDP) is expected in 2013-14; moving to balance in 2015-16 and a surplus of $6.6 billion (0.4 per cent of GDP) in 2016-17.

In accrual terms, a fiscal deficit of $13.5 billion (0.8 per cent of GDP) is expected for 2013-14, moving to a surplus of $6 billion (0.3 per cent of GDP) in 2015-16 and a surplus of $10.8 billion (0.6 per cent of GDP) in 2016-17.

Table 4: Australian Government general government sector budget aggregates

	Actual	Estimates			Projections	
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
	$b	$b	$b	$b	$b	$b
Receipts	**329.9**	**350.4**	**376.0**	**401.2**	**428.9**	**453.6**
Per cent of GDP	22.4	23.0	23.5	23.9	24.3	24.4
Payments(a)	**371.0**	**367.3**	**391.2**	**409.1**	**425.0**	**443.7**
Per cent of GDP	25.2	24.2	24.5	24.4	24.0	23.8
Net Future Fund earnings	2.2	2.5	2.8	2.9	3.1	3.3
Underlying cash balance(b)	**-43.4**	**-19.4**	**-18.0**	**-10.9**	**0.8**	**6.6**
Per cent of GDP	-2.9	-1.3	-1.1	-0.6	0.0	0.4
Revenue	**338.1**	**360.0**	**387.7**	**411.6**	**438.1**	**468.6**
Per cent of GDP	22.9	23.7	24.3	24.5	24.8	25.2
Expenses	**377.7**	**381.4**	**398.3**	**415.7**	**431.0**	**454.7**
Per cent of GDP	25.6	25.1	24.9	24.8	24.4	24.4
Net operating balance	-39.6	-21.5	-10.6	-4.1	7.1	13.8
Net capital investment	4.9	-1.2	2.9	2.2	1.1	3.0
Fiscal balance	**-44.5**	**-20.3**	**-13.5**	**-6.3**	**6.0**	**10.8**
Per cent of GDP	-3.0	-1.3	-0.8	-0.4	0.3	0.6
Memorandum item:						
Headline cash balance	-47.0	-22.2	-25.3	-21.0	-8.6	-3.3

(a) Equivalent to cash payments for operating activities, purchases of non-financial assets and net acquisition of assets under finance leases.
(b) Excludes net Future Fund earnings.

Cash flows

In 2013-14, an underlying cash deficit of $18.0 billion is expected, and a headline cash deficit of $25.3 billion. Table 5 provides a summary of Australian Government general government sector cash flows.

Table 5: Summary of Australian Government general government sector cash flows

	Estimates			Projections	
	2012-13	2013-14	2014-15	2015-16	2016-17
	$b	$b	$b	$b	$b
Cash receipts					
Operating cash receipts	348.8	375.6	398.1	427.2	453.4
Capital cash receipts(a)	1.6	0.4	3.1	1.7	0.2
Total cash receipts	350.4	376.0	401.2	428.9	453.6
Cash payments					
Operating cash payments	359.3	382.4	400.0	416.2	434.5
Capital cash payments(b)	7.5	8.3	9.1	8.7	9.3
Total cash payments	366.9	390.7	409.1	425.0	443.7
Finance leases and similar arrangements(c)	0.4	0.5	0.0	0.0	0.0
GFS cash surplus(+)/deficit(-)	**-16.9**	**-15.2**	**-8.0**	**4.0**	**9.9**
Per cent of GDP	-1.1	-1.0	-0.5	0.2	0.5
less Net Future Fund earnings	2.5	2.8	2.9	3.1	3.3
Underlying cash balance(d)	**-19.4**	**-18.0**	**-10.9**	**0.8**	**6.6**
Per cent of GDP	-1.3	-1.1	-0.6	0.0	0.4
Memorandum items:					
Net cash flows from investments in financial assets for policy purposes	-5.3	-10.1	-13.1	-12.6	-13.2
plus Net Future Fund earnings	2.5	2.8	2.9	3.1	3.3
Headline cash balance	**-22.2**	**-25.3**	**-21.0**	**-8.6**	**-3.3**

(a) Equivalent to cash receipts from the sale of non-financial assets in the cash flow statement.
(b) Equivalent to cash payments for purchases of non-financial assets in the cash flow statement.
(c) The acquisition of assets under finance leases decreases the underlying cash balance. The disposal of assets previously held under finance leases increases the underlying cash balance.
(d) Excludes expected net Future Fund earnings.

Variations to the underlying cash balance estimates

Table 6 provides a reconciliation of the variations in the underlying cash balance since the 2012-13 Budget.

The change in estimated underlying cash balance since MYEFO is largely a result of write-downs in taxation receipts, offset in part by the effect of policy decisions which improve the underlying cash balance by $15.4 billion over the four years from 2012–13.

Table 6: Reconciliation of underlying cash balance estimates

	Estimates			Projections
	2012-13	2013-14	2014-15	2015-16
	$m	$m	$m	$m
2012-13 Budget underlying cash balance(a)	**1,536**	**2,044**	**5,318**	**7,469**
Per cent of GDP	0.1	0.1	0.3	0.4
Changes from 2012-13 Budget to 2012-13 MYEFO				
Effect of policy decisions(b)	1,411	5,121	1,917	1,897
Effect of parameter and other variations	-1,869	-5,000	-3,910	-2,958
Total variations	-458	121	-1,993	-1,061
2012-13 MYEFO underlying cash balance(a)	**1,077**	**2,165**	**3,325**	**6,408**
Per cent of GDP	0.1	0.1	0.2	0.4
Changes from 2012-13 MYEFO to 2013-14 Budget				
Effect of policy decisions(b)(c)				
Receipts	*-56*	*255*	*5,603*	*9,521*
Payments	*2,302*	*975*	*-584*	*-2,803*
Total policy decisions impact on underlying cash balance	-2,358	-720	6,188	12,324
Effect of parameter and other variations(c)				
Receipts(d)	*-16,358*	*-17,024*	*-14,557*	*-15,306*
Payments	*1,738*	*2,464*	*5,843*	*2,576*
Total parameter and other variations impact on underlying cash balance	-18,096	-19,488	-20,400	-17,882
2013-14 Budget underlying cash balance(a)	**-19,377**	**-18,043**	**-10,888**	**849**
Per cent of GDP	-1.3	-1.1	-0.6	0.0

(a) 2012-13 MYEFO and 2013-14 Budget figures exclude expected net Future Fund earnings, whereas 2012-13 Budget figures exclude expected gross Future Fund earnings.
(b) Excludes secondary impacts on public debt interest of policy decisions and offsets from the Contingency Reserve for decisions taken.
(c) A positive number for revenue indicates an increase in the fiscal balance, while a positive number for expenses and net capital investment indicates a decrease in the fiscal balance.
(d) Receipts will differ from the cash receipts reconciliation published in Budget Statement 5 as the table above excludes Future Fund earnings while Statement 5 includes Future Fund earnings.

Changes to receipt estimates since MYEFO

Since the 2012-13 MYEFO, tax receipts have been revised down by $12.9 billion in 2012-13, $16.6 billion in 2013-14 and $61.0 billion over the four years to 2015-16.

Company tax is the single largest contributor to the write-downs in tax receipts. Lower than expected CGT and resource rent taxes have compounded the fall in company tax receipts.

- Of this, company tax receipts account for $5.2 billion in 2012-13, $7.2 billion in 2013-14 and $24.3 billion over the four years to 2015-16. This reflects lower than expected company profitability across most sectors of the economy. Lags in the company tax system mean that lower profitability in 2012-13 will be felt across a number of years.

- Gross resource rent taxes, comprised of minerals resource rent taxes (MRRT) and petroleum resource rent taxes (PRRT), have been written-down significantly compared to the 2012-13 MYEFO. Resource rent taxes are expected to be $3.6 billion lower in 2012-13 and $3.2 billion in 2013-14. These taxes are highly sensitive to the assumptions regarding production volumes, capital deductions, commodity prices and the exchange rate.

- While MRRT receipts have been much lower than expected in 2012-13, they are expected to grow over the forward estimates. MRRT receipts will be supported by very strong increases in production volumes as the economy transitions from the investment phase of the mining boom towards a record expansion in resources production and exports (iron ore exports are expected to grow by around 40 per cent from 2012-13 to 2016-17). In addition, capital expenditure — which can be immediately written off for MRRT purposes — is expected to be lower in the out years than projected at the 2012-13 MYEFO (see Budget Statement 2, Box 8).
- Net MRRT receipts are expected to be around $1.8 billion lower in 2012-13 and $1.7 billion lower in 2013-14.
- PRRT receipts are expected to be weaker across the entire forward estimates, reflecting, in part, a softening in petroleum prices and lower assumed production levels across a number of relevant fields.

• CGT, which is an important component of individuals, companies and superannuation funds tax, is expected to be lower by $1.8 billion in 2012-13 and $2.9 billion in 2013-14, reflecting the continuing utilisation of a large amount of capital losses.

Compared to the 2012-13 MYEFO, carbon pricing mechanism (CPM) receipts are expected to be $140 million higher in 2012-13, largely owing to lower free permit allocations offsetting reduced carbon emissions. Receipts are expected to be $530 million lower in 2013-14; largely reflecting downward revisions to forecast emissions, and the lower international carbon price associated with the advance auctions of permits.

Indirect taxes excluding CPM have been revised down by $760 million in 2012-13, largely reflecting a $515 million write-down of GST and a $900 million downgrade in excise receipts, partly offset by higher customs duties. Indirect taxes, excluding CPM, have been revised down by around $1.4 billion in 2013-14 and $5.2 billion over the four years to 2015-16.

Since the 2012-13 MYEFO, non-tax receipts have declined by $3.7 billion in 2012-13, largely reflecting the deferral of receipts relating to the auction of the digital dividend spectrum, previously anticipated to be received in 2012-13. The timing of final digital dividend receipts was changed in response to industry concern about paying for both the reissue of expiring spectrum licences and spectrum licences won at the digital dividend auction within a short period of time.

Policy decisions since the 2012-13 MYEFO are expected to increase receipts by $255 million in 2013-14, $5.6 billion in 2014-15, $9.5 billion in 2015-16 and $10.1 billion in 2016-17. These decisions include: increasing the Medicare levy to help fund *DisabilityCare Australia*, protecting the integrity of the income tax base, improving the sustainability of the superannuation system and better targeting tax expenditures.

The Medicare levy will be increased by half a percentage point from 1 July 2014 to provide strong and stable funding for *DisabilityCare Australia*. This is expected to increase tax receipts by $11.4 billion over the forward estimates period. All of the monies raised by the additional levy will go directly to the *DisabilityCare Australia* Fund. This fund is expected to generate $467 million in non-tax receipts over the forward estimates period. To assist with establishing *DisabilityCare Australia*, the Government will make a share of the *DisabilityCare Australia* Fund available to States and Territories.

The Budget also contains measures to protect the integrity of the income tax base and promote better tax compliance, including the following:

- the *Protecting the corporate tax base from erosion and loopholes* package contains a series of measures to address abuses that take advantage of design flaws, vulnerabilities and unexpected interactions in the corporate tax law from changes made in the early 2000s. This package is expected to increase tax receipts by $4.1 billion over the forward estimates period;

- providing additional resources to the Australian Taxation Office (ATO) to expand data matching with third party information. This is expected to increase tax receipts by $432 million over the forward estimates period; and

- providing additional resources to the ATO to address risks to the tax system from exploitation of trust structures. This is expected to increase tax receipts by $217 million over the forward estimates period.

Other key revenue measures include the following:

- deferring the Clean Energy Future personal income tax cuts that were scheduled to commence on 1 July 2015. These tax cuts were designed to assist households with the effects of an increase in the carbon price from $25.40 in 2014-15 to $29 in 2015-16. The carbon price in 2015-16 is now projected to be lower ($12.10) than the fixed price in 2014-15. As a result, households will not experience the impact of an additional rise in the carbon price and the 2015-16 tax cuts will be deferred until the carbon price in the Budget is estimated to rise above $25.40. This is currently projected to occur in 2018-19. Households will receive more assistance than was anticipated to be necessary to assist them with the cost of living impact of the carbon price in 2015-16. This measure is expected to increase tax receipts by $1.5 billion over the forward estimates period;

- better targeting support for research and development (R&D) by limiting access to the R&D tax incentive so that it only applies to companies with annual aggregate Australian turnover of less than $20 billion from 1 July 2013. This is estimated to increase tax receipts by $1.1 billion over the forward estimates period;

- extending the requirement to make monthly pay-as-you-go (PAYG) income tax instalments to include all large entities in the PAYG instalment system, including trusts, superannuation funds, sole traders and large investors. This measure is expected to have a gain to tax receipts of $1.4 billion over the forward estimates period;

- phasing out the Net Medical Expenses Tax Offset as reforms to aged care are implemented and *DisabilityCare Australia* is introduced. All existing claimants will be grandfathered for two years, and claims for aged care, disability aids and attendant care will be allowed through until 30 June 2019. This is estimated to increase tax receipts by $968 million over the forward estimates period;

- restructuring the Import Processing Charge to recover the costs of all import related cargo and trade functions undertaken by the Australian Customs and Border Protection Service. This is expected to increase tax receipts by $674 million over the forward estimates period;

- simplifying the design and administration of the proposed higher superannuation concessional contributions cap by providing a $35,000 concessional cap to anyone who meets certain age requirements. This is estimated to increase tax receipts by $365 million over the forward estimates period, as the overall receipts cost of providing the higher cap will fall from $1.5 billion to $1.2 billion;

- better targeting the tax exemption for earnings on superannuation assets supporting retirement income streams, by limiting it to the first $100,000 of annual earnings for each individual, and taxing earnings above that threshold at the concessional rate of 15 per cent. This is expected to increase tax receipts by $356 million over the forward estimates period; and

- indexing tobacco excise to average weekly ordinary time earnings (AWOTE), instead of the CPI. Due to taxpayer confidentiality, this measure has been incorporated into the Budget estimates as a parameter and other variation.

There are also a small number of policy measures since the 2012-13 MYEFO which reduce tax receipts. These include:

- providing petroleum resource rent taxpayers with certainty regarding the scope of deductible expenditure, following recent litigation. This is expected to reduce receipts by $120 million over the forward estimates period; and

- making the superannuation excess contributions tax system fairer by taxing excess concessional contributions at an individual's marginal tax rate plus an interest charge, rather than always taxing them at the top marginal tax rate. This is expected to reduce tax receipts by $55 million over the forward estimates period.

The broader effect on the budget of revisions to the carbon price is outlined in Box 2.

Box 2: Changes to Clean Energy Future Plan

The Government's Clean Energy Future (CEF) Plan is designed to reduce Australia's emissions through a carbon price while supporting households and industry transition to a low-carbon economy.

Starting at $23 in 2012-13, the carbon price is fixed for the first three years until 1 July 2015 when the scheme will transition to a flexible price linked to the European Union (EU) emissions trading scheme. The price in Europe has fallen due in large part to ongoing economic weakness. The flexible carbon price underpinning the 2013-14 Budget has been revised down (see Box 9 in Statement 2).

The carbon price is designed to reduce emissions at a low cost as part of global efforts to improve environmental outcomes. It was not designed to bolster the budget. While the price varies with market movements under an emissions trading scheme, there is a hard cap on the amount of net carbon emissions across the economy. A lower carbon price implies a lower cost to businesses and a lower impact on consumer prices.

Taking into account updated emissions estimates, the revised permit price is estimated to reduce carbon price revenue by around $6 billion over the four years to 2015-16, offset by automatic adjustments and other related policy changes. The overall impact on the fiscal balance is broadly budget neutral over the four years to 2015-16. On the same basis, carbon price receipts are estimated to be $3.7 billion lower over the four years to 2015-16. Taking into account the related changes in this Budget, the net negative impact on the underlying cash balance is around $1 billion over the four years to 2015-16.

Significant elements of industry assistance in the CEF Plan will move in line with changes in the carbon price. These elements include permit based assistance to emissions-intensive, trade-exposed entities under the Jobs and Competitiveness Program, support for electricity generators under the Energy Security Fund and assistance provided through the Coal Sector Jobs Package. The value of assistance under these programs is estimated to be reduced by around $3.9 billion over the four years to 2015-16, in line with the lower carbon-related costs they face.

The CEF Plan included a range of household assistance measures, including tax cuts and increases in pensions, allowances, family payments and other benefits. The household assistance remains in place and the value of payments will be maintained by the normal indexation arrangements. To the extent the carbon price in 2015-16 falls below what had previously been projected, households will receive more assistance than was anticipated to be necessary to assist with the cost of living impact of carbon pricing.

Box 2: Changes to Clean Energy Future Plan (continued)

The Government has decided, however, to defer the CEF personal income tax cuts scheduled to commence on 1 July 2015. There will be no change to the tax cuts applied from the 2012-13 income year.

The additional tax cuts from 1 July 2015 were intended to provide assistance for low and middle income households for a projected increase in the carbon price to $29 in 2015-16, from the fixed price of $25.40 in 2014-15. As the carbon price in 2015-16 is now projected to be lower than $25.40 these tax cuts will be deferred until the carbon price estimated in the Budget is above $25.40. Based on current projections, the carbon price is estimated to be above $25.40 in 2018-19. The Government will continue to monitor the carbon price to ensure the adequacy of household assistance is consistent with its commitments and will bring forward the additional tax cuts should the carbon pricing outlook change earlier than projected.

The Government has also made some decisions to refine particular CEF programs. The Australian Renewable Energy Agency, the Clean Technology Program and the Biodiversity Fund will all have funding adjusted, including to extend the life of the programs over a longer period. The overall level of funding for the clean technology programs has not changed and ARENA funding will remain at over $3 billion over the life of the program.

With the lower projected carbon price, the level of funding for some programs, such as the Carbon Capture and Storage Flagships and the National Low Emissions Coal Initiative, has been reduced. Calls for support from the Regional Structural Adjustment Assistance program have been negligible and this program will not continue.

As part of the second commitment period under the Kyoto Protocol, the Government has elected to include abatement from additional land based activities to count towards Australia's international targets. Farmers and landholders will now be able to sell a wider range of carbon credits to liable entities under the carbon pricing mechanism.

Payment policy decisions since MYEFO

Since MYEFO, total cash payments for 2013-14 have increased by $3.4 billion, comprised of new policy decisions which have increased payments by $975 million and parameter and other variations which have increased payments by $2.5 billion.

Major policy decisions since MYEFO that have increased cash payments in 2013-14 and over the five years to 2016-17 include:

- the *Better Schools: A National Plan for School Improvement* package. These measures will deliver a new school funding system to ensure that every Australian school has the necessary funds to give students the support they need. The cost of these measures assumes the acceptance by all states and territories and non-government school education authorities of the proposed school funding reforms. These measures are expected to increase payments to schools by $473 million in 2013-14 ($9.8 billion over six years from 2014-15);

- implementing *DisabilityCare Australia*, the national disability insurance scheme, to be jointly funded by Commonwealth, State and Territory governments, which will mean that, for the first time, Australians with significant and permanent disability will get the support they need, when they need it. *DisabilityCare Australia* will provide eligible participants with reasonable and necessary support tailored to their individual circumstances in South Australia (for young children), Tasmania (for young adults), the Hunter in New South Wales, and the Barwon area of Victoria from 1 July 2013, and in the Australian Capital Territory and the Barkly region of the Northern Territory from 1 July 2014. *DisabilityCare Australia* will provide state-wide coverage in New South Wales, South Australia and the Australian Capital Territory by 1 July 2018 and in Victoria, Queensland, Tasmania and the Northern Territory from 1 July 2019. This measure is expected to increase Commonwealth payments by $27 million in 2013-14 ($14.3 billion over the seven years from 2012-13 until full implementation, including funding in the 2012-13 budget);

- a number of new and amended listings on the Pharmaceutical Benefits Scheme and the Repatriation Pharmaceutical Benefits Scheme, which are expected to increase payments by $139 million in 2013-14 ($682 million over the five years to 2016-17);

- continuing, in 2013-14, Australia's contribution to international stabilisation and counter-terrorism in Afghanistan and the Middle East Area of Operations. This measure is expected to increase payments by $534 million in 2013-14 ($586 million over the five years to 2016-17); and

- the Royal Commission into Institutional Reponses to Child Sexual Abuse. This measure is expected to increase payments by $130 million in 2013-14 ($434 million over the five years to 2016-17).

The impact of these policy decisions on payments has been more than offset over the five years to 2016-17 by a number of decisions that have reduced cash payments, including:

- a range of changes to Family Tax Benefit (FTB) payments, including not proceeding with the 2012-13 Budget measure *Spreading the Benefits of the Boom*; changing the financial support arrangements for families following the birth or adoption of a child; and continuing the current indexation pauses on upper income thresholds and supplements. Changes to family payments are expected to decrease overall payments by $349 million in 2013-14 ($4.3 billion over the five years to 2016-17);
- offering Student Start-up Scholarships as income contingent loans, rather than as grants, to all new full-time higher education students in receipt of Youth Allowance, Austudy or ABSTUDY from 1 January 2014. This measure is expected to decrease payments by $35 million in 2013-14 ($1.2 billion over the five years to 2016-17);
- applying an efficiency dividend of 2.0 per cent in 2014 and 1.25 per cent in 2015 to most grants provided under the *Higher Education Support Act 2003*. This measure is expected to decrease payments by $85 million in 2013-14 ($903 million over the five years to 2016-17, although funding is still projected to grow by $1.1 billion over this period);
- removing the discounts applying to up-front payments and voluntary repayments under the Higher Education Loan Program from 1 January 2014. This measure is expected to decrease payments by $34 million in 2013-14 ($267 million over the five years to 2016-17);
- realigning indexation of the Medicare Benefits Schedule to the financial year. This measure is expected to decrease payments by $151 million in 2013-14 ($653 million over the five years to 2016-17); and
- deferring the commitment to 0.5 per cent of Gross National Income on Official Development Assistance by one year to 2017-18. This measure is expected to decrease payments by $1.9 billion over the five years to 2016-17. Under this new profile, ODA spending is forecast to grow by 42.4 per cent from 2013-14 across the forward estimates.

Further details of Government policy decisions are provided in Budget Paper No. 2, *Budget Measures 2013-14*. The expense estimates provided in Budget Paper No. 2 are in accrual terms and may not align exactly with the underlying cash payment figures provided in this Statement.

Payment estimates variations since MYEFO

This Budget also incorporates some major changes in expected payments in 2013-14 as a result of parameter and other variations since MYEFO.

Major increases in expected payments in 2013-14 as a result of parameter and other variations since MYEFO include:

- payments under the Natural Disaster Relief and Recovery Arrangements, which are expected to be $219 million higher in 2013-14 ($1.9 billion over the four years to 2015-16), primarily relating to relief and recovery payments for the floods in early 2013 in Queensland and northern New South Wales;
- Research and Development Tax Incentive payments, which are expected to be $135 million higher in 2013-14 ($574 million over the four years to 2015-16), largely reflecting higher than expected large claims in the first year of operation of the 2009-10 Budget measure *An Innovation and Higher Education System for the 21st Century — Research and Development Tax Credit*. It is expected that a higher level of claims will continue across the forward estimates;
- offshore asylum seeker management costs, which are expected to be $1.3 billion higher in 2013-14 ($3.2 billion over the four years to 2015-16), reflecting updated projections of irregular maritime arrivals and the cost of regional processing centres;
- Private Health Insurance payments, which are expected to increase by $474 million in 2013-14 ($2.2 billion over the four years to 2015-16), largely reflecting stronger than expected growth in the number of people with subsidised private health cover and more people upgrading their level of health insurance. Around 55 per cent of Australians now have some form of private health cover, the largest proportion in over 20 years;
- Medicare Benefits Schedule (MBS) payments, which are expected to be $454 million higher in 2013-14 ($2.1 billion over the four years to 2015-16), reflecting growth in the use of medical services owing in part to increases in the primary care workforce and in the use of high value items on the MBS;
- official development assistance eligible expenses associated with irregular maritime arrivals, which are expected to be $431 million higher in 2013-14 ($943 million over the four years to 2015-16), reflecting updated projections of irregular maritime arrivals. The Government will cap the amount of expenditure in the ODA budget that can be reprioritised for ODA eligible IMA expenses at $375 million per year;
- payments of Family Tax Benefit (FTB), which are expected to be $276 million higher in 2013-14 ($1.0 billion over the four years to 2015-16), largely reflecting higher than previously projected recipient numbers, payment rates and top-up payments made after the lodgement of tax returns; and
- Youth Allowance payments for unemployed youth, which are expected to increase by $125 million in 2013-14 ($423 million over the four years to 2015-16), reflecting a higher than expected number of recipients continuing to receive income support.

Major reductions in expected payments in 2013-14 as a result of parameter and other variations since MYEFO, include:

- payments under the Pharmaceutical Benefits Scheme (PBS), which are expected to be $176 million lower in 2013-14 ($1.1 billion over the four years to 2015-16), reflecting the impact of price disclosure in line with the agreement reached with industry in 2010, which progressively reduces the price of some PBS medicines that are subject to competition;

- Veterans' Affairs payments, which are expected to be $75 million lower in 2013-14 ($409 million over the four years to 2015-16), reflecting a forecast natural decline in the number of beneficiaries across a range of programs;

- Tertiary Student Assistance payments, which are expected to be $376 million lower in 2013-14 ($979 million over the four years to 2015-16). This is largely related to the 2011-12 Budget measure, *Supporting Families with Teenagers*, which is designed to align the system so that FTB-A will be the primary payment for full-time students and Youth Allowance for those out of school. This has resulted in a decrease in client numbers for Youth Allowance;

- Income Support for Carers payments, which are expected to be $115 million lower in 2013-14 ($509 million over the four years to 2015-16), largely reflecting lower than expected growth in recipient numbers; and

- Low Income Supplement (LIS) payments, which are expected to be $141 million lower in 2013-14 ($497 million over four years to 2015-16). In 2012-13, the LIS had a smaller than projected customer take-up and it is forecast that low customer numbers will continue as the eligible population is expected to remain stable.

Consistent with previous budgets, the underlying cash balance has been improved by the regular draw down of the conservative bias allowance. Details of this draw down are provided in Appendix B of Statement 6, *Expenses and Net Capital Investment*.

Fiscal balance estimates

The fiscal deficit is expected to be $13.5 billion (0.8 per cent of GDP) in 2013-14, a change of $17.8 billion since the $4.3 billion surplus expected in MYEFO.

Table 7 provides a reconciliation of the variations in the fiscal balance since the 2012-13 Budget.

Table 7: Reconciliation of fiscal balance estimates

	Estimates			Projections
	2012-13	2013-14	2014-15	2015-16
	$m	$m	$m	$m
2012-13 Budget fiscal balance	**2,500**	**2,646**	**7,020**	**9,457**
Per cent of GDP	0.2	0.2	0.4	0.5
Changes from 2012-13 Budget to 2012-13 MYEFO				
Effect of policy decisions(a)	386	5,852	2,442	2,424
Effect of parameter and other variations	-1,679	-4,222	-2,539	-2,118
Total variations	-1,293	1,629	-97	305
2012-2013 MYEFO fiscal balance	**1,207**	**4,275**	**6,923**	**9,762**
Per cent of GDP	0.1	0.3	0.4	0.5
Changes from 2012-13 MYEFO to 2013-14 Budget				
Effect of policy decisions(a)(b)				
Revenue	-36	111	5,533	9,766
Expenses	1,978	382	-1,014	-3,054
Net capital investment	63	196	356	87
Total policy decisions impact on fiscal balance	-2,077	-467	6,191	12,733
Effect of parameter and other variations(b)				
Revenue	-13,742	-15,523	-15,792	-18,108
Expenses	4,413	65	2,973	-1,742
Net capital investment	1,242	1,717	605	174
Total parameter and other variations impact on fiscal balance	-19,396	-17,306	-19,370	-16,540
2013-14 Budget fiscal balance	**-20,266**	**-13,497**	**-6,255**	**5,955**
Per cent of GDP	-1.3	-0.8	-0.4	0.3

(a) Excludes secondary impacts on public debt interest of policy decisions and offsets from the Contingency Reserve for decisions taken.
(b) A positive number for revenue indicates an increase in the fiscal balance, while a positive number for expenses and net capital investment indicates a decrease in the fiscal balance.

Changes in revenue estimates since MYEFO

Changes in accrual revenue are generally driven by the same factors as cash receipts, though differences arise where revenue raised in a given year is not received in that year.

Changes in expense estimates since MYEFO

Movements in accrual expenses over the forward estimates are broadly similar to the movements in cash payments. The key exceptions include:

- superannuation benefits, where there are differences between the timing of cash payments and accrued expenses; and
- the Natural Disaster Relief and Recovery Arrangements, where expenses are recognised in the financial year in which the disaster occurs, rather than when cash payments are made.

More detailed information on expenses can be found in Statement 6, *Expenses and Net Capital Investment*.

Net capital investment estimates

Net capital investment is broadly defined as the sale and acquisition of non-financial assets less depreciation expenses. It provides a measure of the overall growth in capital assets (including buildings and infrastructure, specialist military equipment, and computer software) after taking into account depreciation and amortisation as previously acquired assets age.

In 2013-14, net capital investment is forecast to be $1.9 billion higher than forecast in MYEFO, largely reflecting the acquisition of military equipment and the construction of Defence support facilities as outlined in the 2013 Defence White Paper. Capital investment in 2013-14 includes payments for 12 new-build EA-18G Growler aircraft, three Air Warfare Destroyers, and two Landing Helicopter Dock amphibious ships, the replacement of Australia's Armidale Class Patrol Boats and continued investment in the development of fifth-generation F-35A Joint Strike Fighter aircraft.

More detailed information on net capital investment can be found in Statement 6, *Expenses and Net Capital Investment*.

Net debt, net financial worth and net worth

The Government's medium-term fiscal strategy commitment to achieve surpluses, on average, over the medium term, assists in reducing net debt over time as a share of GDP. The medium-term fiscal strategy also commits to improving the Government's net financial worth over the medium term.

Table 8 provides a summary of Australian Government general government sector net financial worth, net worth, net debt and net interest payments.

The large write-downs in tax receipts in 2012-13 and over the forward estimates have contributed to budget deficits out to 2014-15, necessitating a higher borrowing requirement. This has, in turn, resulted in higher net debt, and lower net worth and net financial worth than forecast at MYEFO.

Table 8: Australian Government general government sector net worth, net financial worth, net debt and net interest payments

	Estimates			Projections	
	2012-13	2013-14	2014-15	2015-16	2016-17
	$b	$b	$b	$b	$b
Financial assets	242.2	264.0	286.0	308.8	343.0
Non-financial assets	110.3	112.6	115.1	116.9	119.1
Total assets	**352.5**	**376.6**	**401.1**	**425.8**	**462.2**
Total liabilities	**513.6**	**550.1**	**577.0**	**593.9**	**618.1**
Net worth	**-161.1**	**-173.5**	**-175.9**	**-168.2**	**-156.0**
Net financial worth(a)	**-271.4**	**-286.1**	**-290.9**	**-285.1**	**-275.1**
Per cent of GDP	-17.8	-17.9	-17.3	-16.1	-14.8
Net debt(b)	**161.6**	**178.1**	**191.6**	**191.2**	**185.7**
Per cent of GDP	10.6	11.1	11.4	10.8	10.0
Net interest payments	**8.2**	**7.8**	**8.4**	**9.8**	**7.7**
Per cent of GDP	0.5	0.5	0.5	0.6	0.4

(a) Net financial worth equals total financial assets minus total liabilities.
(b) Net debt equals the sum of deposits held, government securities, loans and other borrowing, minus the sum of cash and deposits, advances paid and investments, loans and placements.

Net debt for the Australian Government general government sector is estimated to be $178.1 billion (11.1 per cent of GDP) in 2013-14, $33.5 billion higher than estimated at MYEFO.

The increase in 2013-14 net debt since MYEFO is primarily driven by a higher issuance of Commonwealth Government Securities, which has been partly offset by an increase in the value of certain investments held by the Future Fund.

Australian Government net debt continues to remain low by international standards. The average net debt for the major advanced economies is expected to peak at around 92.6 per cent of GDP in 2014, whilst Australia’s net debt will peak at 11.4 per cent of GDP in 2014-15. Australia’s net debt position is then expected to reduce to 10.0 of GDP by 2016-17.

The changes to net debt described above also impact on net financial worth and net worth.

- Net financial worth is estimated to be –$286.1 billion in 2013-14, compared to the MYEFO estimate of -$251.5 billion.

- Net worth is forecast to be –$173.5 billion in 2013-14, compared to the MYEFO estimate of -$138.3 billion.

Improving the government’s balance sheet over the medium term provides the Government with the capacity and flexibility to respond to unanticipated adverse events and longer-term challenges.

Further details on the balance sheet are outlined in Statement 7, *Asset and Liability Management.*

Medium-term fiscal outlook

Table 9 outlines the underlying cash balance and net debt across the medium term. On current projections, there is an underlying cash surplus of $21.4 billion by 2023-24.

Table 9: Medium-term projections

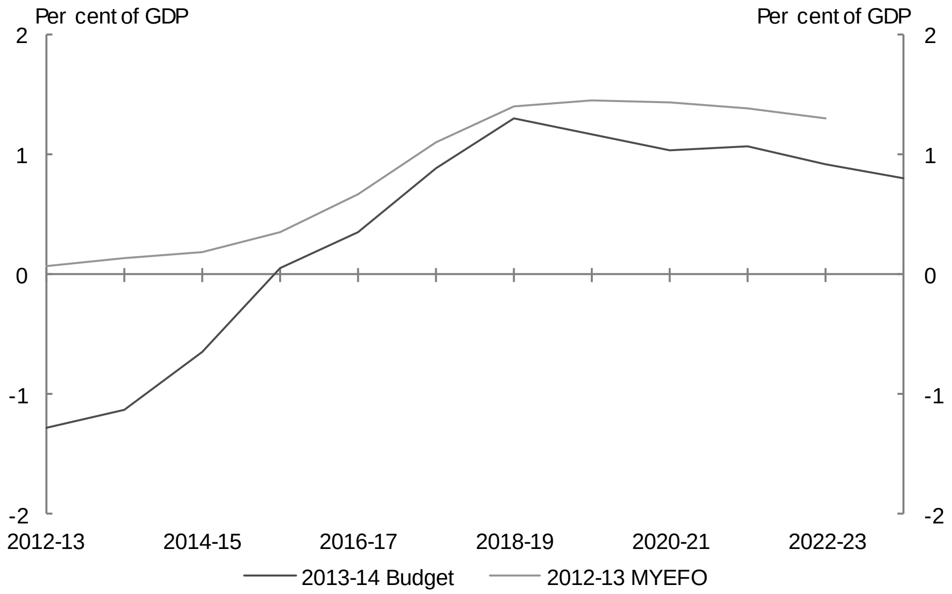
	Medium-term projections						
	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24
Underlying cash balance ($b)(a)	**18**	**27**	**26**	**24**	**26**	**24**	**21**
Per cent of GDP	0.9	1.3	1.2	1.0	1.1	0.9	0.8
Net Debt ($b)	**150**	**106**	**69**	**30**	**-5**	**-38**	**-68**
Per cent of GDP	7.6	5.1	3.2	1.3	-0.2	-1.5	-2.5

(a) Excludes expected net Future Fund earnings.
Note: In addition to the underlying cash balance, changes in net debt include increases in the value of the non-equity assets of the Future Fund due to earnings and capital gains, and changes in the market value of debt.

The medium term fiscal projections reflect the Government's fiscal strategy. Real growth in spending is assumed to be held to 2 per cent a year, on average, until the underlying cash surplus is at least 1 per cent of GDP and while the economy is growing at or above trend. The level of tax receipts is allowed to return naturally as the economy grows until it reaches 23.7 per cent of GDP (2018-19). That ratio is then held constant.

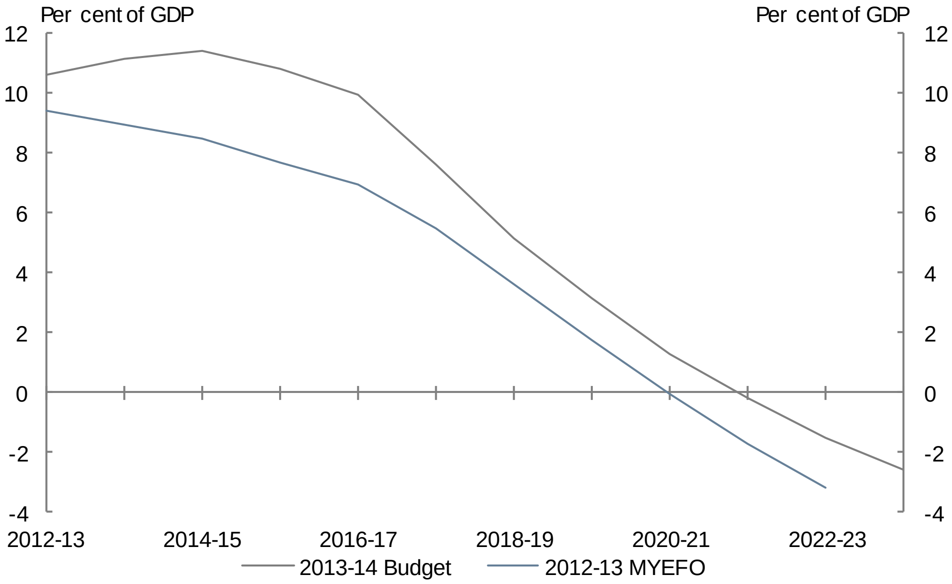
On current projections, the underlying cash balance is expected to reach 1 per cent of GDP in 2018-19, one year later than projected at MYEFO (Chart 3). Net debt is projected to return to zero in 2021-22, one year later than projected at MYEFO (Chart 4). This delay is mainly attributable to the weaker outlook for the underlying cash balance.

Chart 3: Underlying cash balance projected to 2023-24



Source: Treasury projections.

Chart 4: Government net debt projected to 2023-24



Source: Treasury projections.

APPENDIX A: SENSITIVITY OF BUDGET ESTIMATES TO ECONOMIC DEVELOPMENTS

The estimates contained in the 2013-14 Budget are based on forecasts of the economic outlook. Changes to the economic assumptions underlying the estimates will impact on receipts and payments, and hence the size of the underlying cash balance.

This section examines the effects on receipts and payments of altering some of the key economic assumptions. Tables A2 and A4 illustrate the sensitivity of key components of receipts and payments to possible variations in the economic outlook. The two scenarios considered are:

- Scenario 1: a 1 per cent reduction in nominal GDP owing to a fall in the terms of trade.

- Scenario 2: a 1 per cent increase in real GDP driven by an increase in labour productivity and labour force participation, with each contributing equally.

The economic scenarios provide a rule of thumb indication of the impact on receipts, payments and the underlying cash balance of changes in the economic outlook. They represent a partial economic analysis only and do not attempt to capture all the economic feedback and other policy responses related to changed economic conditions. In particular, the analysis assumes no change in the exchange rate, interest rates or policy over the forecast period. The impact of the two scenarios on the economic parameters would be different if the full feedback response on economic variables and likely policy actions were taken into account. The analysis does not aim to provide an alternative picture of the economic forecasts under these scenarios, but instead gives an indication of the sensitivity associated with different components of receipts and payments to changes in the economy. As such, the changes in the economic variables and their impact on the fiscal outlook are merely illustrative.

The impacts shown in the tables below are broadly symmetrical. That is, impacts of around the same magnitude, but in the opposite direction, would apply if the terms of trade were to increase or if real GDP were to decrease.

Scenario 1

The first scenario involves a permanent fall in world prices of non-rural commodity exports in 2013-14 consistent with a fall in the terms of trade of around 4 per cent, which causes a 1 per cent fall in nominal GDP by 2014-15. The sensitivity analysis evaluates the flow-on effects on the economy, the labour market and prices. The impacts in Table A1 are stylised and refer to per cent deviations from the baseline levels of the economic parameters.

Table A1: Illustrative impact of a permanent non-rural commodity price fall consistent with a 1 per cent fall in nominal GDP by 2014-15 (per cent deviation from the baseline level)

	2013-14 per cent	2014-15 per cent
Real GDP	0	- 1/4
Non-farm GDP deflator	- 3/4	- 3/4
Employment	- 1/4	- 1/2
Wages	0	- 1/4
CPI	0	- 1/4
Company profits	-3	-3
Consumption	- 1/4	- 1/2

Assuming no change in exchange rates or interest rates, the fall in export prices leads directly to a lower non-farm GDP deflator (from the export component of GDP) and lower domestic incomes. Lower domestic incomes cause both consumption and investment to fall, resulting in lower real GDP, employment and wages. The fall in aggregate demand puts downward pressure on domestic prices.

In reality, a fall in the terms of trade would be expected to lead to a fall in the exchange rate, although the magnitude is particularly uncertain in the short term. In the event of a fall in the exchange rate, the impacts on the external sector would dampen the real GDP effects, and there would be some offsetting upward pressure on domestic prices.

Given these assumptions, the overall impact of the fall in the terms of trade is a decrease in the underlying cash balance of around $3.1 billion in 2013-14 and around $5.7 billion in 2014-15 (see Table A2).

Table A2: Illustrative sensitivity of the budget balance to a 1 per cent decrease in nominal GDP due to a fall in the terms of trade

	2013-14 $b	2014-15 $b
Receipts		
Individuals' and other withholding taxation	-0.6	-1.4
Superannuation funds taxation	-0.1	-0.3
Company tax	-2.0	-3.1
Resource rent taxes	-0.3	-0.5
Goods and services tax	-0.1	-0.2
Excise and customs duty	0.0	-0.1
Other taxation	0.0	0.0
Total receipts	**-3.1**	**-5.6**
Payments		
Income support	-0.1	-0.2
Other payments	0.0	0.1
Goods and services tax	0.1	0.2
Total payments	**0.0**	**0.1**
PDI	0.0	-0.2
Underlying cash balance impact	**-3.1**	**-5.7**

On the receipts side, a fall in the terms of trade results in a fall in nominal GDP which reduces tax collections. The largest impact is on company tax receipts as the fall in export income decreases company profits. Owing to lags in the tax system, the effect on company tax is larger in 2014-15. Lower company profits are assumed to flow through to lower Australian equity prices, therefore reducing capital gains tax from individuals, companies and superannuation funds.

The weaker economy results in lower aggregate demand, which flows through to lower employment and wages, reducing individuals' income tax receipts. The decrease in disposable incomes leads to lower consumption, which in turn results in a decrease in GST receipts (decreasing GST payments to the states by the same amount) and other indirect taxes.

On the payments side, a significant proportion of government expenditure is partially indexed to movements in costs (as reflected in various price and wage measures). Some forms of expenditure, in particular income support payments, are also driven by the number of beneficiaries.

The overall estimated expenditure on income support payments (including pensions and allowances) increases in both years because of a higher number of unemployment benefit recipients. The increase in unemployment benefits in 2014-15 is partly offset by reduced expenditure on pensions and allowances reflecting lower growth in benefit rates resulting from lower wages growth and lower inflation. At the same time other payments linked to inflation fall in line with the reduced growth in prices.

The reduction in the underlying cash balance results in a higher borrowing requirement and a higher public debt interest cost.

As noted above, under a floating exchange rate, the fall in the exchange rate would damp the effects of the fall in the terms of trade on real GDP, meaning the impact on the fiscal position could be substantially more subdued. Also, to the extent that the fall in the terms of trade is temporary rather than permanent, the impact on the economic and fiscal position would be more subdued.

Scenario 2

The second scenario involves a permanent 0.5 per cent increase in both the participation rate and labour productivity, resulting in a 1 per cent increase in real GDP in 2013-14. Once again, the sensitivity analysis evaluates the flow-on effects on the economy, the labour market and prices. The impacts in Table A3 are stylised and refer to per cent deviations from the baseline levels of the parameters.

The 1 per cent increase in real GDP increases nominal GDP by slightly less but the magnitude of the effects on receipts, payments and the underlying cash balance differ from the first scenario because different parts of the economy are affected in different ways.

Table A3: Illustrative impact of an ongoing equal increase in both labour productivity and participation consistent with a 1 per cent increase in real GDP in 2013-14 (per cent deviation from the baseline level)

	2013-14 per cent	2014-15 per cent
Nominal GDP	3/4	3/4
Non-farm GDP deflator	- 1/4	- 1/4
Employment	1/2	1/2
Wages	1/4	1/4
CPI	- 1/4	- 1/4
Company profits	1 3/4	1 3/4
Consumption	1	1

The increases in labour force participation and labour productivity have the same impact on output, but different impacts on the labour market. Higher productivity leads to higher real GDP and higher real wages, while an increase in the participation rate increases employment and real GDP. Imports are higher in this scenario, reflecting higher domestic incomes.

Since the supply side of the economy expands, inflation falls relative to the baseline. The lower domestic prices make exports more attractive to foreigners, with the resulting increase in exports offsetting higher imports, leaving the trade balance unchanged. The exchange rate is assumed to be unchanged.

The overall impact of the increase in labour productivity and participation is an increase in the underlying cash balance of around $3.1 billion in 2013-14 and around $4.1 billion in 2014-15 (see Table A4).

Table A4: Illustrative sensitivity of the budget balance to a 1 per cent increase in real GDP due to an equal increase in both productivity and participation

	2013-14 $b	2014-15 $b
Receipts		
Individuals' and other withholding taxation	1.7	1.6
Superannuation funds taxation	0.1	0.3
Company tax	1.2	1.8
Goods and services tax	0.5	0.5
Excise and customs duty	0.2	0.2
Other taxation	0.0	0.0
Total receipts	**3.7**	**4.4**
Payments		
Income support	-0.1	-0.1
Other payments	0.0	0.1
Goods and services tax	-0.5	-0.5
Total payments	**-0.6**	**-0.5**
PDI	0.0	0.2
Underlying cash balance impact	**3.1**	**4.1**

On the receipts side, individuals' income tax collections increase because of the rise in the number of wage earners and, additionally, higher real wages. The stronger labour market also increases tax collections from superannuation funds because contributions (including compulsory contributions) are higher. The increase in personal incomes leads to higher consumption which results in an increase in GST receipts (with the corresponding receipts passed on in higher GST payments to the states). In addition, the stronger economy results in higher levels of corporate profitability, increasing company taxes.

On the payments side, overall estimated expenditure on income support payments (including pensions and allowances) is slightly higher primarily reflecting growth in benefit rates through their indexation to wages. Lower inflation has a partially offsetting effect.

On balance, the rise in estimated tax collections is only partially offset by increased payments. This improves the underlying cash position, which results in a lower borrowing requirement and lower public debt interest cost.

To the extent that the increases in productivity and participation are temporary rather than permanent, the impact on the economic and fiscal position would be more subdued.