

Solid Budget foundations confirmed Pre-election Economic and Fiscal Outlook (PEFO)

- The PEFO report has confirmed that a small budget deficit is expected in 2018/19 with a small surplus expected in 2019/20.

The independent PEFO report must be handed down before a Federal Election is held.

What does it all mean?

- An independent assessment of the Budget position has to be provided ahead of the Federal Election. The Department of Finance notes: *“The Charter of Budget Honesty Act 1998 requires the secretaries of the Department of Treasury and the Department of Finance to release a pre-election report that provides updated information on the economic and fiscal outlook. The PEFO report must be released within 10 days of the issue of the writ for a general election.”*
- Given that the Budget was handed down just over two weeks ago, few changes were expected in the PEFO. And indeed that is the case. *“The economic and fiscal outlook for the Commonwealth has not materially changed since the publication of the 2019-20 Budget on 2 April 2019. An underlying cash surplus of \$7.1 billion (0.4 per cent of GDP) is expected in 2019-20, with further surpluses expected across the forward estimates.”*

What do the figures show?

- The budget is expected to be in deficit by \$4.3 billion in the current year (2018/19). The 2019 Budget forecast a \$4.2bn deficit. A budget surplus of \$7.1 billion is expected in 2019/20.
- The only change in the key aggregates since the budget has been a lift in payments in 2018/19 from \$482.7 billion to \$482.8 billion.
- PEFO says *“Real GDP is forecast to grow at around its estimated potential rate of 2% per cent in 2019-20 and 2020-21, sustaining solid employment growth and supporting a pick-up in wage growth.”*
- The PEFO report provides a reconciliation of the underlying cash balance estimates from the 2019/20 Budget to the 2019 PEFO.
- *“Policy decisions taken since the 2019-20 Budget have had a negative underlying cash balance impact of \$93 million in*

	Estimates			Projections		Total(a)
	2018-19	2019-20	2020-21	2021-22	2022-23	
	\$m	\$m	\$m	\$m	\$m	\$m
2019-20 Budget underlying cash balance(b)	-4,162	7,054	11,004	17,792	9,165	45,014
Per cent of GDP	-0.2	0.4	0.5	0.8	0.4	
Changes from 2019-20 Budget to 2019 PEFO						
Effect of policy decisions(c)(d)						
Receipts	0	-3	0	0	0	-3
Payments	93	0	1	0	0	0
Total policy decisions impact on underlying cash balance	-93	-2	-1	0	0	-3
Effect of parameter and other variations(d)						
Receipts	0	2	12	0	0	14
Payments	0	2	12	0	0	14
less Net Future Fund earnings(e)	0	0	na	na	na	0
Total parameter and other variations impact on underlying cash balance	0	0	0	0	0	0
2019 PEFO underlying cash balance(b)	-4,254	7,051	11,003	17,792	9,165	45,011
Per cent of GDP	-0.2	0.4	0.5	0.8	0.4	
Memorandum:						
Net Future Fund earnings(e)	6,592	5,140	5,207	5,563	6,249	22,159

(a) Total is equal to the sum of amounts from 2019-20 to 2022-23.

(b) Excludes expected net Future Fund earnings before 2020-21.

(c) Excludes secondary impacts on public debt interest of policy decisions and offsets from the Contingency Reserve for decisions taken.

(d) A positive number for receipts improves the underlying cash balance, while a positive number for payments worsens the underlying cash balance.

(e) Under the Future Fund Act 2006, net Future Fund earnings will be available to meet the Australian Government's superannuation liability in 2020-21. From this time, the underlying cash balance includes expected net Future Fund earnings.

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2018-19 and \$3 million over the four years to 2022-23. This primarily reflects the decision to extend the Energy Assistance Payment to additional welfare payments, which is expected to increase payments by \$88 million in 2018-19.”

- **Decisions since the 2019 Budget serve to reduce expenses** by \$300,000 in 2019/20; increase expenses by \$1.1m in 2020/21 and increase expenses by \$1.4m in the following two years.
- **Decisions since the 2019 Budget serve to reduce revenues** by \$2.4 million in 2019/20; increase revenues by \$600,000 in 2020/21 and increase revenues by \$3.2m in the following two years.
- **The estimated net impact over the four years to 2022-23 of all unlegislated policy decisions**, announced prior to the PEFO and after taking account of parameter changes since the original announcement, is around negative \$1.4 billion in underlying cash terms. This comprises:
 - policy decisions made prior to the 2019-20 Budget that require legislation to be implemented, which have a net positive impact on the underlying cash balance of around \$5.4 billion over the four years to 2022-23; and
 - new policy decisions announced in the 2019-20 Budget that require legislation to be implemented, which have a net negative impact on the underlying cash balance of around \$6.9 billion over the four years to 2022-23. This includes policy decisions with an estimated net negative impact of \$1.4 billion that require annual appropriation bills but do not require any other enabling legislation to be implemented.
- **There are a number of tax measures included in the 2019-20 Budget that take effect on or before 1 July 2019.** Many of these measures can be legislated at a later time within 2019-20 without materially affecting the estimates. However, the immediate relief to low- and middle-income earners component of the “Lower taxes for hard-working Australians: Building on the Personal Income Tax Plan” measure requires the relevant legislation to be passed before the increase to the low and middle income tax offset (LMITO) can be provided for the 2018-19 financial year. If not legislated prior to 1 July 2019, the revenue cost of this measure would need to be reassessed.
- **Estimates of net debt, net financial worth, net worth and net interest payments have not materially changed since the 2019-20 Budget.** In 2019-20, net debt for the Australian Government general government sector is expected to be \$361.1 billion (18 per cent of GDP) and is projected to decline to zero per cent of GDP by 2029-30.
- Overall in the 2019 PEFO, the Contingency Reserve estimates reduce expenses by \$2.0 billion in 2018-19 and \$222 million in 2019-20, and increase expenses by \$2.1 billion in 2020-21, \$4.3 billion in 2021-22 and \$9.0 billion in 2022-23.

What is the importance of the economic data?

- The heads of the **Department of Finance and Federal Treasury** jointly release the Pre-Election Economic and Fiscal Outlook report within 10 days of the calling of a Federal Election.
- “PEFO makes public any decision of Government since the last economic update was published. The update ensures that the government, the opposition, the parliament and the public know the country’s fiscal position before the election.”
- “In contrast to the other financial reports published each year by the government, the PEFO is prepared independently by the Secretaries of the Departments of Finance and the Treasury and is released under their names without consulting with the government. They also publish costings prepared by the Treasury and Finance on election commitments that have been requested by political parties in the lead up to a federal election.”

What are the implications for interest rates and investors?

- There have been few changes to the fiscal estimates made in the 2019 Budget. The Government is aiming to provide stimulus through tax cuts and infrastructure spending. However the value and impact of the stimulus will depend on when the legislation is passed.
- CommSec expects interest rates to be unchanged for the foreseeable future. But the loss of momentum across global economies means central banks are skewed to more accommodative monetary policies.

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