Part I: Overview

The fiscal outlook remains largely unchanged since the publication of the 2002-03 Budget, despite an expected moderation in economic growth associated with the drought and the weaker global environment.

An underlying cash surplus of $2.1 billion is anticipated in 2002-03, unchanged from the 2002-03 Budget estimate. A slight fall in expected cash payments is offset by a slight downward revision to expected cash receipts. Solid taxation collections in recent months point to a broadly unchanged revenue outcome for the year, even after factoring in the expected impact of slower economic growth. Table 1 presents the fiscal and underlying cash balances for 2002-03 and the forward years.

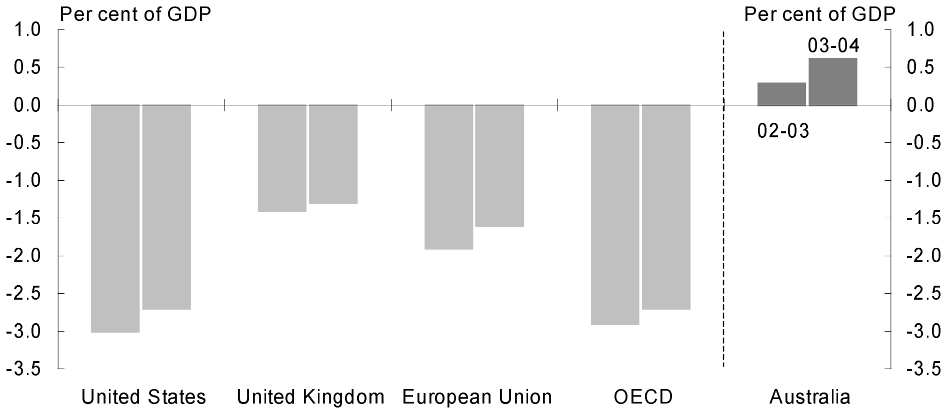
Table 1: Summary of budget aggregates[(a)]

	2002-03		2003-04	
	Budget	MYEFO	Budget	MYEFO
Underlying cash balance ($b)	**2.1**	**2.1**	**3.7**	**4.9**
Per cent of GDP	0.3	0.3	0.5	0.6
Fiscal balance ($b)	**0.2**	**-0.5**	**2.6**	**3.4**
Per cent of GDP	0.0	-0.1	0.3	0.4
	2004-05		2005-06	
	Budget	MYEFO	Budget	MYEFO
Underlying cash balance ($b)	**4.6**	**4.2**	**7.1**	**5.4**
Per cent of GDP	0.6	0.5	0.8	0.6
Fiscal balance ($b)	**5.0**	**4.2**	**7.7**	**5.8**
Per cent of GDP	0.6	0.5	0.9	0.7

(a) Estimated surpluses for 2004-05 and 2005-06 include a downward revision due to changes made to the medium-term economic projections since Budget. See page 17 of Part II.

The underlying cash surpluses projected for the future years emphasise Australia's sound fiscal outlook, with most OECD countries currently experiencing significant deficits.

Chart 1: International comparison of budget balances 2003 and 2004[(a)]



(a) International data are for the total general government sector, sourced from *OECD Economic Outlook (72) (preliminary edition, November 2002)*. Australian data is for the Commonwealth general government sector.

The slight fall in estimated cash payments in 2002-03 is largely due to favourable parameter and other variations offsetting policy measures announced since the 2002-03 Budget. These measures include: support for Australian victims of the Bali terrorist attacks and their immediate families; enhancements to Australia's security following the Bali attacks; an immunisation programme against the Meningococcal C virus; and the Medical Indemnity Insurance Assistance Package.

Although estimated receipts for 2002-03 remain virtually unchanged from Budget, the composition of expected growth has changed. Forecast income tax receipts from wage and salary earners have been revised downwards, while anticipated company and other individuals taxation receipts have been revised upwards.

In accrual terms, the fiscal balance is expected to record a small deficit in 2002-03, before returning to surplus in 2003-04. This reflects timing differences between when revenues and expenses are recognised and when they are recorded in cash terms. For example, superannuation expenses in 2002-03 are expected to be higher than cash payments. Further details on the accrual and cash budget estimates are provided in Part III.

DOMESTIC AND INTERNATIONAL ECONOMIC OUTLOOK

The Australian economy is expected to grow by around 3 per cent in 2002-03, a downward revision to the 3¾ per cent growth rate forecast at Budget. The downward revision of ¾ of a percentage point is mainly due to the expected effects of the drought on the economy. Other parts of the economy are expected to continue to grow solidly. Non-farm GDP is forecast to grow by 3¾ per cent in 2002-03, unchanged from Budget.

The positive outlook for the domestic economy is against a backdrop of a weak and highly uncertain global environment. Global economic conditions have remained subdued since Budget and downside risks around the outlook have heightened. World growth is expected to be around 2¾ per cent in 2002, unchanged from the Budget forecast, but the forecast for 2003 has been revised down to 3½ per cent, from 4 per cent at Budget.

The fragile global economic environment clouds an otherwise sound domestic outlook. Although there are some domestic risks to the Australian outlook — particularly uncertainty around the severity of the drought and the expected adjustment in the housing sector – the main risk is the possibility of prolonged international weakness, which would undermine confidence and spending, and exacerbate the domestic risks.

Domestic demand is forecast to increase by 4¾ per cent in 2002-03, underpinned by solid consumption growth and a strong pick-up in business investment. However, net exports are expected to subtract 1¾ percentage points from growth, with the substantial downward revision since Budget largely reflecting the expected effects of the drought on farm production and incomes, and the weaker global environment.

Employment growth is forecast to be 1¾ per cent in 2002-03 in year-average terms and the unemployment rate is forecast to decline through the year to around 6 per cent in the June quarter 2003 in line with the Budget forecasts. The Consumer Price Index is forecast to increase by about 2¾ per cent in 2002-03 in year-average terms, with inflation pressures remaining subdued.

The initial forecast for 2003-04 is for economic growth to rebound to 4 per cent. This forecast assumes a return to average seasonal conditions in rural Australia and stronger world growth. Non-farm GDP growth is expected to be a little slower than in 2002-03 reflecting the expected slowdown in dwelling construction. There are, however, substantial risks around the outlook and a weaker outcome is possible if the dry conditions persist or if global economic conditions deteriorate further.