# OVERVIEW

The Government is on track to achieve a modest budget surplus within the forward estimates, while at the same time ensuring the economy is supported in the short term with accommodating fiscal policy, and in the longer term with new policy directions to lift productivity, economic growth, and therefore Australian living standards now and into the future.

With moderate unemployment, contained inflation, and low public debt, Australia currently has some of the strongest economic fundamentals in the developed world (Table 1).

**Table 1: Major economic parameters(a)**

| | Forecasts | | Projections | |
|---|---|---|---|---|
| | 2013-14 | 2014-15 | 2015-16 | 2016-17 |
| Real GDP | 2 1/2 | 3 | 3 | 3 |
| Employment | 1 | 1 1/2 | 1 1/2 | 1 1/2 |
| Unemployment rate | 6 1/4 | 6 1/4 | 5 | 5 |
| Consumer Price Index | 2 1/2 | 2 | 2 1/2 | 2 1/2 |
| Nominal GDP | 3 3/4 | 4 1/2 | 5 1/4 | 5 1/4 |
| Terms of trade | -5 3/4 | -3 3/4 | -1 1/2 | -1 1/2 |

(a) Real and nominal GDP are year average growth. Employment and CPI are through-the-year growth to the June quarter. The unemployment rate is the rate in the June quarter.
Source: ABS cat. nos. 5206.0, 6202.0 and 6345.0, Treasury.

While prospects remain favourable, the economic outlook has softened further since the Budget, particularly for nominal GDP. The outlook for world growth has weakened, including in China, and the world price of key commodities has fallen leading to lower forecast terms of trade. This, along with lower forecast real GDP growth and a weaker outlook for wage growth, has led to a substantial downgrade to nominal GDP growth over the forecast period.

Nominal GDP is now forecast to grow by 3¾ per cent in 2013-14 and 4½ per cent in 2014-15, well below its 20-year average of 6½ per cent. This, in turn, has had a major impact on expected tax receipts, which, since Budget, have been revised down as a result of the softer economic outlook by $33.3 billion over the forward estimates.

**Table 2: Summary of budget aggregates**

| | Estimates | | Projections | |
|---|---|---|---|---|
| | 2013-14 | 2014-15 | 2015-16 | 2016-17 |
| **Underlying cash balance ($b)(a)** | **-30.1** | **-24.0** | **-4.7** | **4.0** |
| Per cent of GDP | -1.9 | -1.5 | -0.3 | 0.2 |
| **Fiscal balance ($b)** | **-25.6** | **-22.2** | **1.8** | **7.6** |
| Per cent of GDP | -1.6 | -1.4 | 0.1 | 0.4 |

(a) Excludes net Future Fund earnings.

The Government remains committed to the medium-term fiscal strategy that has steered Australia's successful response to the Global Financial Crisis, and which provides the basis for the Government's decision to keep the budget on track to return to surplus and keep Australia's fiscal position strong (Table 2).

The Government has already undertaken a significant fiscal consolidation since 2009-10. It is now using the flexibility in the fiscal strategy to respond to the changes in the economic outlook, while strengthening fiscal sustainability in the medium term. The Government has ensured that the pace of fiscal consolidation carefully balances the importance of a sustainable fiscal position with the risks to jobs and growth that have been seen internationally from too fast a consolidation.

With the economy currently facing a period of transition and falling terms of trade, cuts in the near term to offset the lower than expected tax receipts and other variations in the budget would put jobs and growth at risk. With the forecast moderate slowdown, and the unemployment rate expected to increase slightly over the next year, the Government has made the clear decision to allow the tax write-downs to flow through to the budget balance in 2013-14 and 2014-15. As a result, the expected deficit in 2013-14 is now $30.1 billion, and the expected deficit in 2014-15 is $24.0 billion.

From 2015-16 more significant savings take effect and mostly offset the slower growth in tax receipts so that there is a modest deficit in 2015-16 and a modest surplus in 2016-17. The Government considers that these savings can be managed while maintaining growth in jobs and the broader economy.

A medium-term consolidation and path back to budget surplus is appropriate to strengthen medium-term budget sustainability, and is made possible by Australia's strong economic fundamentals. The Government has made $17.4 billion of responsible savings decisions to provide a pathway to expected surplus in 2016-17. The majority of the required consolidation is planned to occur in 2015-16 and 2016-17 when the economic transition is further progressed, allowing for a pick-up in the pace of consolidation. The savings decisions make a significant structural improvement to the Government's fiscal position over the medium and longer term.

Preliminary estimates indicate that the underlying cash deficit in 2012-13 will be around $18.8 billion (around 1.2 per cent of GDP), which suggests a slightly improved outcome from previous estimates. The final results for 2012-13 will be determined following the finalisation of audit cleared financial statements and will be published in the 2012-13 Final Budget Outcome by 30 September 2013.

## MANAGING THE TRANSITION

Over the past decade, the resources sector has been a major contributor to Australian economic growth. Increasing demand for Australia's mineral and energy resources pushed up export prices and prompted a massive expansion of investment in iron ore, coal and LNG projects. This combination of higher prices and increased investment in the resources sector resulted in a period of very strong income growth for Australia.

This abnormal period of heavy reliance on one part of the economy will come to an end, and managing the transition back to more normal, broader based growth will be a key economic challenge over the next few years. The prices of Australia's resource exports peaked in 2011 and have fallen since then. While the level of investment is expected to remain at historically elevated levels over the forecast period, investment in iron ore and coal projects has probably already peaked, with future investment underpinned by LNG projects already under construction. Economic growth will increasingly depend on renewed growth in other sectors of the economy, like manufacturing, tourism and services.

Australia embarks on this transition from a position of strength with some of the strongest economic fundamentals in the developed world.

As the transition unfolds, the Australian economy is forecast to grow by a solid 2½ per cent in 2013-14 and 3 per cent in 2014-15. To ensure that the transition is as smooth as possible, we must preserve and build upon Australia's strengths as an open, flexible and competitive economy. But even with relatively smooth growth, it is likely that export prices will continue to fall over the medium term as the global supply of resources increases.

In these circumstances, higher productivity growth will be the key to improving living standards.

In response, the Government has committed to a new National Competitiveness Agenda, to lift productivity, economic growth, and Australian living standards now and into the future. The Government is working cooperatively with business and the unions to lift Australia's annual productivity growth rate to 2 per cent or better. This collaborative approach maximises the opportunity that significant productivity-enhancing reforms can be agreed and implemented.