National Australia Bank

2014-15 Federal Budget

14 May 2014

Comment	The Budget faced significant new outlays in coming years in the area of National Disabilities, Gonski education reforms and Paid Parental Leave. This Budget should really be seen as a re-ordering of Budget priorities to fund these commitments and at the same time put the Budget on a more robust path to balance. With net debt to GDP of around 17% this was never a budget in crisis – albeit it did face medium term challenges. The Government has opted to spread the pain and start straight away. Much of that pain has been well signaled. That included tightening eligibility criteria for family tax benefits and eligibility rules for unemployment benefits: increased cuts to public sector employment (from 12000 to 16500): merger/abolishion of 70 public entities and resort to more privatization; a deficit tax levy of 2% for those paid more than $180k per annum (for three years); cuts to industry assistance programs worth $850m; resumption of petrol indexation (with the proceeds put to road funding);and medical co-payment of $7 per visit (to set up a new medical services future fund); large cuts to hospital payments: and university fee liberalisation (which will increase the cost of some courses). In the longer run; Gonski funding from 2018 will be replaced by an indexation of education funding; the pension age will be raised to 70 years effective from 2035 and pension assets test will not be indexed for a number of years. See section on Budget Measures. Over the next three years the measures represent significant saves (around $15bn) – with most of the work done on the revenue side. Effectively our estimates suggest that the Government, in a structural sense, is taking around ½% out of growth in each year in the forward estimates. While the tax rises and petrol tax increases are not enough to seriously impact growth, they together with significant transfer cuts could well have more important impacts on confidence. See Medium Term Fiscal Context. On the Budget forecasts' Nab is more optimistic on growth (Nab 3% Govt 2 ½% in 2014/15). That said we are more cautious on domestic demand reflecting a view that public sector demand and/or consumption might be hit harder by Budget announcements. That said the Government sees unemployment peaking at the same rate as Nab, but staying at that rate longer (all of 2015/16). They also see a faster terms of trade fall and hence lower nominal GDP growth. Overall we see the forecasts as unlikely to overstate the fiscal outcome and indeed they appear marginally conservative. Clearly this Budget has lots of politics. And it is there that the main uncertainties arise. How many of the measures announced will get through the Parliament and what will the measures do to consumer and business confidence?
Fiscal Outcome	The underlying cash deficit for 2013/14 is estimated at $49.9 billion (3.1% percent of GDP). The Budget maintains large, but shrinking, deficits of $29.8 billion in 2014/15, $17.1 billion in 2015/16, and $10.6 billion in 2016/17. The government has set an objective to return the Budget to a 1% of GDP over the medium-term
Economic Outlook	The Government's economic outlook is softer than recent RBA forecasts, and slightly softer than NAB's forecasts for 2014-15 (NAB is weaker in 2015/16). In 2014/15, the government is forecast real GDP growth of 2½% (compared to NAB's 3.1%), reflecting a smaller trade balance that more than offsets their stronger expectation for domestic demand. In 2015/16, the Governments forecast is a little stronger (3% compared to NAB's 2.7%) due to an anticipated improvement in domestic demand (NAB are forecasting a further slowing, led by a contraction in mining investment). The Government expects unemployment to rise to around 6¼% by mid 2015, while NAB expects it to peak sooner (at a similar level), before easing to around 6%. The Government, RBA and NAB share very similar views on the outlook for underlying inflation, although the RBA see larger price pressures in the near-term. Each expects inflation to remain well within the RBA's 2-3% target band over the forecast horizon. The structural adjustment occurring in the economy at present remains a real risk to the outlook. Nothing in the Budget changes our view that rates are on hold until late 2015. For further details, see the *Economic and Financial Outlook.*
Financial Markets	Beyond the economic/fiscal outlook, the budget was regarded to be 'credit positive' by Moody's, and supportive of Australia's AAA rating. The market reaction to the Budget was positive, with the $A quickly rising ½ a cent to under 0.938, before retracing. Despite all the concern in the lead up, most measures were well flagged with no real negative surprises. Overall, the market sees the budget as a good start towards addressing the looming structural pressures facing government finances.

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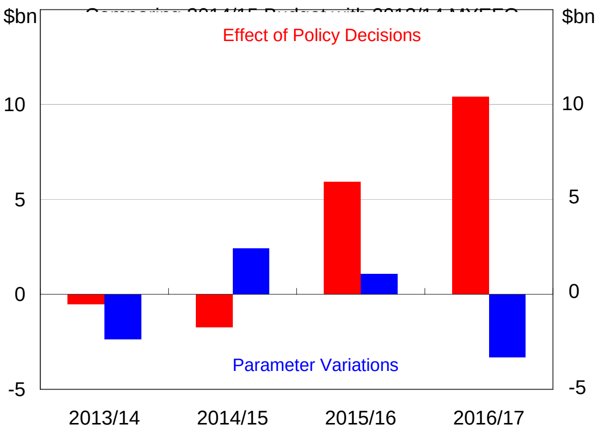
Medium Term Fiscal Context

As noted earlier, the Budget does involve significant policy tightening. This can be seen in the following chart which compares the relevant contribution from policy vis a vis the economic cycle.

Reasons for Change in the Budget Cash Balance



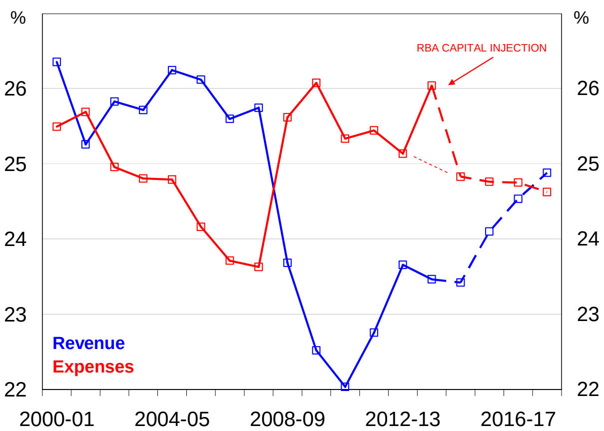
Source: Commonwealth Treasury

The chart also highlights the point that the really significant saves come in 2015/16 and beyond.

Also the heavy lifting has mainly been done from the revenue side. This is also evident if we look at the Budget "jaws" (i.e. revenue versus outlays as a percentage of GDP). As a per cent of GDP there is a steady, but modest, lowering of expenses (ex the RBA capital injection this financial year). However the real turnaround kicks in 2015/16 as the full year impact of the deficit levy, the medical co-payment, petrol excise and foreign aid reductions all kick in.

Commonwealth revenue & expenses*

% of GDP



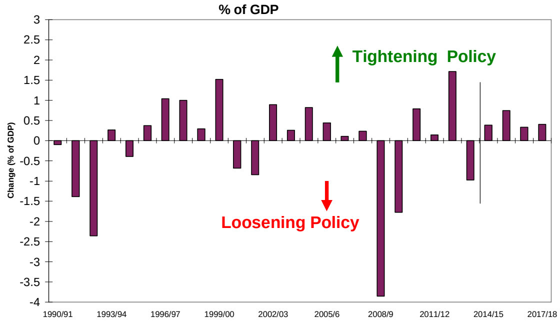
Sources: ABS; Commonwealth Treasury; NAB calculations; RBA

* GST classified as Commonwealth tax & expense

Using OECD methodology the implication is that over the forward estimates period the Budget is effectively taking around ½% out of growth in each year – with slightly more (around ¾%) in 2015/16.

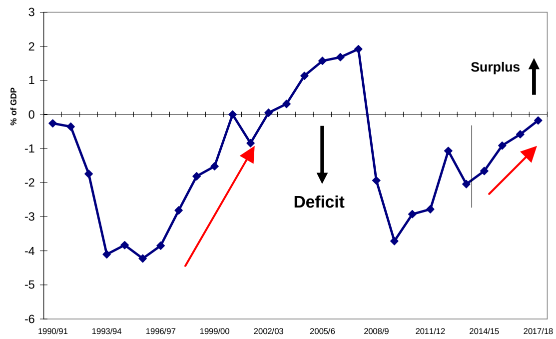
Structural impluse - Change from the Budget to the Economy

% of GDP



That means that by 2017/18 the Structural deficit is approaching balance. Also it is worth noting that the chart shows that the Howard / Costello fiscal consolidation was more aggressive than the current consolidation phase. That makes sense as the 1990s period did not see implementation of large spending programs such as National Disability, Gonski, and Paid Parental Leave Schemes

Structural Budget Balance - % of GDP

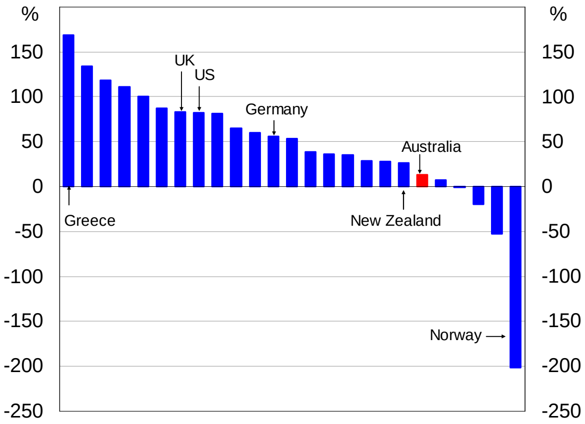


On the credibility of the forecasts, as noted above, while we have differences in some areas - such as weaker domestic demand, lower unemployment in the out years and stronger terms of trade – overall we have no fundamental queries re the credibility of the fiscal and economic projections. Indeed the lower nominal GDP estimates suggest there may well be a degree of conservatism in the forecasts (unlike recent Budget history)

That said, at least Australia starts from a good fiscal starting point, as highlighted by the following international comparison chart of public net debt to GDP. A similar conclusion can be seen in the International Forecasting section below where it is clear Australia did not suffer a blow out in spreads and or come under pressure from rating agencies.

Net Government Debt in Advanced Economies

Per cent of GDP; 2013



Source: World Economic Outlook Database

Budget Measures – In Brief

In accrual terms, the fiscal deficit for 2013/14 is estimated to be $45.1 bn (or 1.6% of GDP). Key highlights of spending and saving measures (those committed within the current Budget period) include:

New Spending Initiatives

Infrastructure:

- New investment of $11.6bn. On our estimates around 35,000 direct jobs over the medium term (and more via indirect effects).

Business

- Industry Skills Fund: From 1 January 2015, the government will establish a training fund for SMEs, allocating $476 million over four years to support specialised training programs.

Revenue Measures

Company Tax

- 1.5% reduction in company tax to 28.5% (July 2015). But there is a reduction in Government assistance programs ($850m)

Personal income tax

- Deficit levy (above 180k per annum +2% increase in marginal rate raising $3bn over 3 years)

Fuel Excise Indexation

- Petrol excise indexation (but no change to diesel rebate for farmers / miners). To be hypothecated to road building. Raises around $2bn

Saving Measures

Family

- Tighter eligibility criteria for welfare (Family tax benefit B threshold reduced and unemployed less than 25 years to youth allowance) and raising pension age to 70 (by 2035)

Education

- Gonski funding cut from 2018 – to be replaced by indexation funding increases
- University fee liberalisation (effective increased fees at least for some courses) with changes to the provision of Commonwealth funding leading to savings.

Foreign Aid

- Foreign aid reduced over the forecast period equal to over $7 billion in savings.

Public Sector Consolidation

- Cuts to public sector employment (was 12000 now 16500)
- Merger of 70 Government agencies & privatisation (eg Australian Mint,)

Social Assistance

- Pension age to increase to 70 by 2035; indexation of pensions to inflation, cessation of seniors supplement worth $1.1bn, counting super in Seniors Health Card eligibility to save $20m

Health

- Doctor and hospital co-payment charge ($7 per visit). $2 to doctors and the rest hypothecated to new Medical Research Future Fund – building to $20bn over 6 years. Large cuts to hospital funding building through time.
- Changes to costs of PBS medicines and Safety Net thresholds. Combined, these measures will save $1.3 billion over four years.

Economic & Financial Outlook

Global outlook

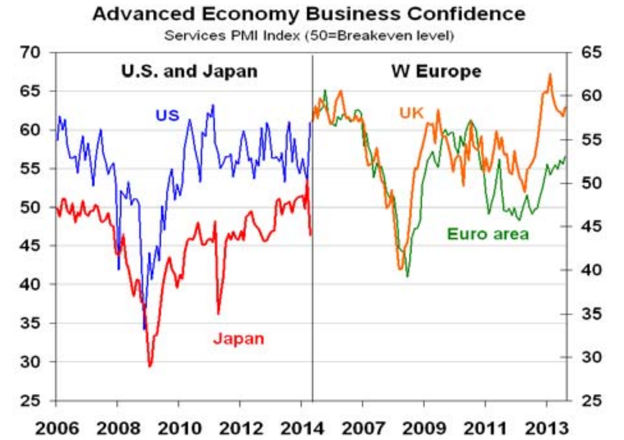
Treasury expects global growth to accelerate from 3% in 2012/13 to 3½% in 2013/14 and then settle at an around trend 3¾% through the following two years. We have similar numbers with the main difference being we expect a more marked slowing in Chinese growth through the forecast period.

Comparison of Treasury Budget Forecasts and NAB Forecasts

	2013/14		2014/15		2015/16	
	Tsy	NAB	Tsy	NAB	Tsy	NAB
US	2.75	2.4	3	2.9	3	2.8
Euro-zone	1	1.3	1.5	1.4	1.5	1.6
Japan	1.5	1.4	1	1.3	1	1.1
China	7.25	7.3	7.25	7	7	6.8
India	4.75	5.2	5.25	5.6	5.5	6.1
Emerging Asia	4.5	4.1	4.5	4.3	4.75	4.5
World	***3.5***	***3.5***	***3.75***	***3.7***	***3.75***	***3.8***
Major trading part	4.75	4.6	4.75	4.6	4.75	4.5

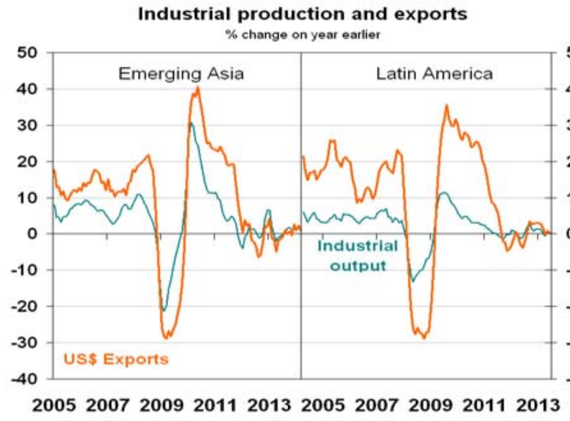
Treasury takes a mainstream view of the forces shaping global activity and the resulting pattern of growth differences between countries. Treasury agrees with recent IMF and OECD assessments showing accelerating growth in the big advanced economies and a mixed picture among the big emerging market economies (slowing trend in China alongside recovery toward more normal rates of growth in India and Brazil). The charts below illustrate how the rebalancing of growth toward advanced economies is already well under way.

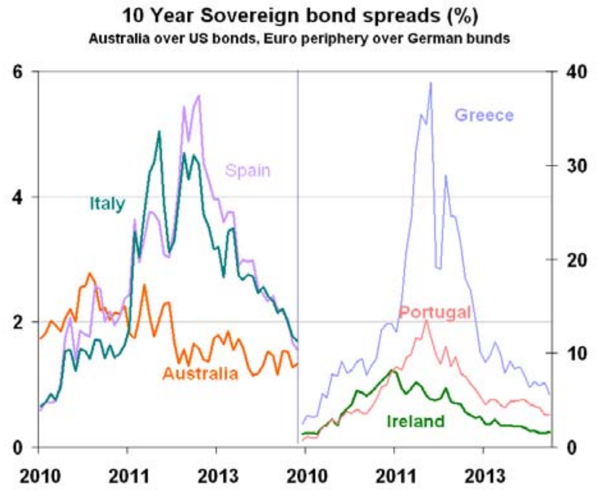
The monthly business surveys of purchasing managers (PMIs) across the big advanced economies give the most up to date reading of how they are recovering from the deep recession of 2008/9. GDP in the G7 advanced economies took almost four years to recover to its early 2008 level and it was still only 3% above that level at the end of 2013. The PMIs show recovery in Western Europe and the US continuing through early 2014 but the recent rise in Japanese consumption taxes has clearly hit spending. Outside Japan, other long-running national business surveys show firms expect the moderate upturn to continue. Japanese growth should slow towards its very low long run potential rate as "Abenomics" stimulus wears off.



While recovery in the advanced economies has been proceeding as expected, the emerging market economies that dominate our export markets have experienced a bumpier road. A combination of interest rate rises to combat higher inflation, the very modest pace of growth in world trade, financial market volatility linked to expectations of eventually increasing US interest rates and political tensions have hit growth in several big economies.

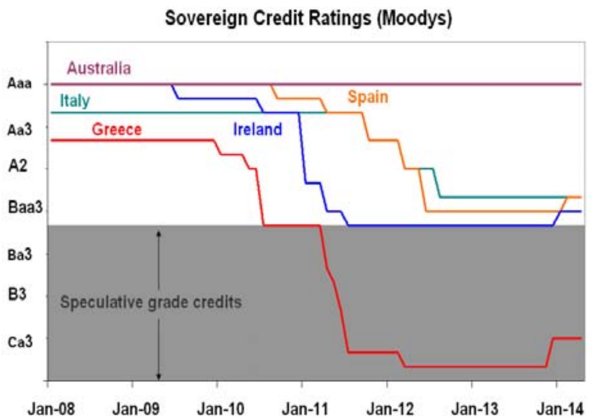
Neither the hard data on trade and industrial output in the emerging markets nor their national business surveys show any recent evidence of acceleration in growth. This minimal industrial and trade growth across Emerging Asia and Latin America in early 2014 is shown in the chart below. Nevertheless, we and Treasury are expecting performance across India and East Asia (excluding Japan and China) to gradually improve through the forecast horizon.





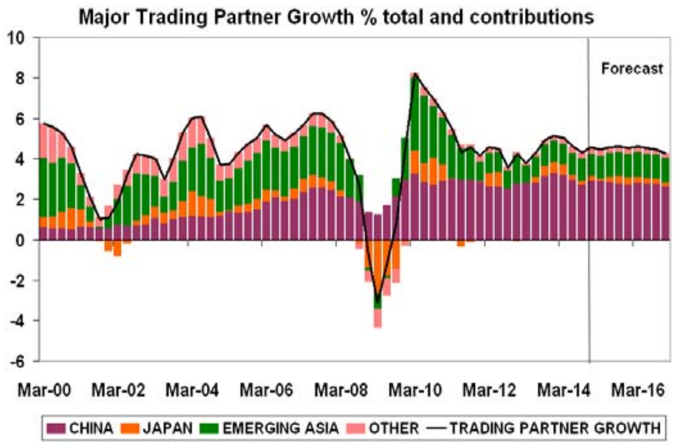
Although the pace of recovery in the big advanced economies has been moderate, one of the most encouraging features of the global economic environment has been the reduced threat of "tail risks" – a lower chance of seeing really bad economic outcomes whose occurrence could derail the global recovery.

Despite all the fears about over-capacity, unsustainable growth and property bubbles, we and Treasury see the Chinese economy experiencing a gradual slowdown rather than the feared "hard landing". Concern that the Euro-zone could fragment or that important member states could default on their sovereign debt has also abated. The profile of sequential cuts in Euro-zone peripheral countries' credit ratings and their widening bond spreads through 2010 to 2012 shows what normally happens in a "fiscal emergency". The situation improved drastically after the ECB Governor's 2012 speech where he said the central bank would do "whatever it takes" to prevent a collapse of the Euro monetary union.



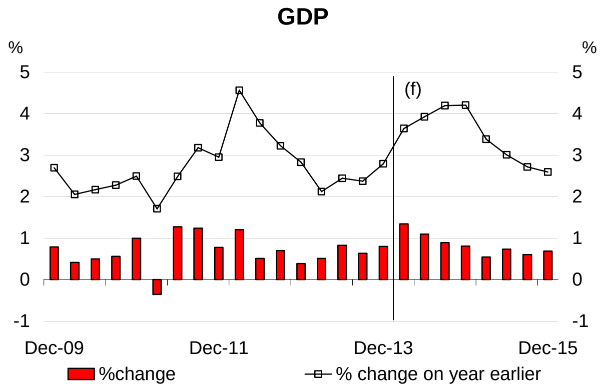
The Australian economy has become increasingly dependant on China which now buys almost 40% of our merchandise exports. China is second to New Zealand in overseas arrival numbers and is the biggest buyer of our educational service exports.

The importance of China for recent and future growth in demand for Australian products is evident in the chart of major trading partner growth shown below. Even through we and Treasury forecast Chinese growth to slow through the next few years, it still gives almost two-thirds of the increase in Australian export-weighted global demand and "emerging East Asia" contributes most of the rest.



Australian outlook

The Commonwealth Treasury's Budget papers note that the global economic outlook has improved, but the Australian economy is in the midst of a major structural transformation, with the resource boom moving out of the investment phase and into the exports and production phase. The fall in resource investment is likely to be lumpy, and uncertainty over the timing of these phases are a risk to the outlook – at a time when the domestic economy has generally been growing below trend with unemployment rising. In this environment, they note that the scale and timing of the anticipated recovery in non-resources business investment is a major source of uncertainty. These headwinds, combined with further declines in the terms of trade, will continue to weigh on nominal GDP growth and government revenue. Finally, they note that steps to improve the budget bottom line will not have a material impact on growth due to offsetting infrastructure spending.



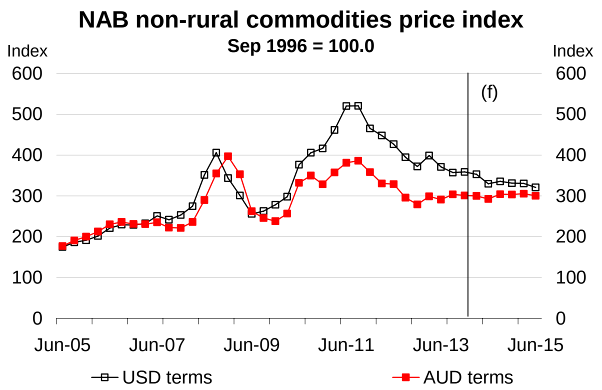
Sources: ABS, NAB estimates

Economic growth has lifted closer to trend in recent quarters, supported by a combination of stronger exports and fewer capital imports. The shift to the next phase of the mining boom – as capital investments become operational and begin to export – appears to be the primary driver of this trend. Real GDP grew by 0.8% in the December quarter, which is close to trend, but this number obscures the weakness of domestic demand (at just 0.1%) that is doing very little to alleviate the current slack in the labour market. Private investment was the weakest area of domestic demand, contracting in the quarter, while tighter fiscal policies are keeping the contribution from the public sector subdued as well. Private consumption improved towards the end of 2013, to record moderate through-the-year growth, but a stronger pick up is needed.

Partial indicators generally suggest that these trends have continued into 2014. Mining investment is set to fall sharply, yet historically low interest rates appear to have done very little to lift non-mining investment due to persistently high levels of spare capacity. However, strong growth in housing prices has encouraged large numbers of building approvals, many of which should have commenced in Q1 and are expected to contribute to solid dwelling investment growth over coming quarters. Retail trade has also showed some positive signs early in the year as rising household wealth (largely through property prices) seemed to more than offset soft labour market conditions. However, with property markets showing some signs of cooling and households seemingly becoming more concerned over the economic outlook and job security, the pace of retail sales has eased.

On a more positive note for businesses, the NAB monthly business survey has shown a notable improvement over the past 6-12 months. First, confidence lifted sharply following the federal election in September, while conditions eventually started to follow suit. However, conditions are still pointing to quite soft business activity. The most recent monthly survey showed a significant weakening in forward orders – a leading indicator of activity. Nevertheless, the NAB survey measures of intended capital expenditure over the next 12 months are looking more positive, despite still subdued levels of capacity utilisation in most industries.

Weighing up all these factors, we see GDP growth remaining below trend in 2014 (but accelerating in 'through the year' terms), as larger contributions from net exports and dwelling investment offset the continuing pull back in business investment – driven by sharply slowing mining investment. However, the impact from faster dwelling investment is expected to wash-out after around 12-months as an elevated unemployment rate puts a brake on property prices and new investment. GDP growth will not be sufficient to prevent the unemployment rate edging up a little further this year.

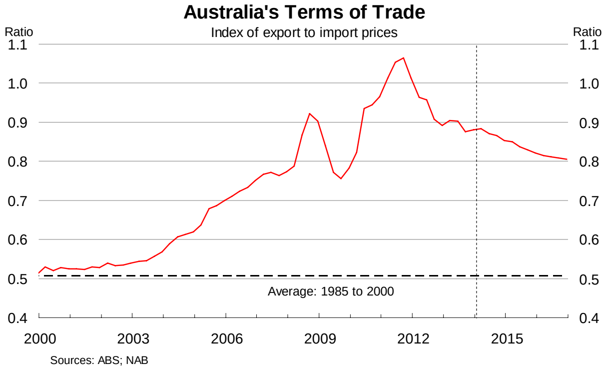


Source: ABS; ABARES; Bloomberg; NAB; Thomson Datastream

The peak in mineral & energy prices is now well behind us and the terms of trade is expected to continue its decline for some time yet, creating a significant headwind to national income. Global demand has remained tepid, particularly as growth in major trading partner China continues to slow.

Conditions facing other trading partners are also mixed. Overall, demand for Australian exports is facing headwinds at a time when supplies of some commodities are picking up considerably. Prices of iron ore have resumed their decline recently, while coking and thermal coal prices have remained at very low levels, rendering a significant share of production unprofitable. With supply conditions looking unfavourable in a number of markets, we expect minerals and energy commodities prices to ease further in USD terms, contributing to a 3½% decline in the terms of trade over 2013/14, and a further 3¾% decline over 2014/15. Nevertheless, the drop in export prices is expected to be more than offset by a step up in resource export volumes (net exports further contributing via lower capital imports). Given the associated contribution to Australian domestic income, NAB expects GDP growth to rise from 2.4% over 2012/13 to 3.2% over 2013/14, before easing to 2.8% over 2014/15.

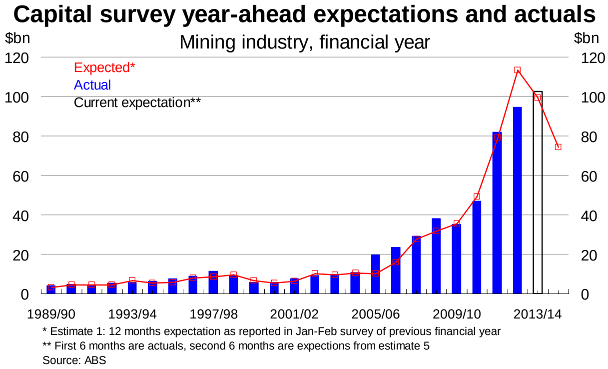
Australia's Terms of Trade



Sources: ABS; NAB

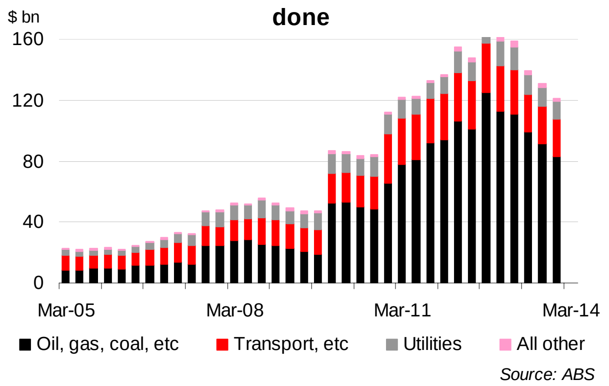
In contrast to net exports, business investment has gone from being a major driver of growth in recent years to a significant drag on the economy more recently. The ABS New Private Capital Expenditure Survey showed a sharp contraction in total capital expenditure of 5.2% in the December quarter. However, the main point of interest from the survey was the first read on firm's investment intentions for 2014/15. Using five year average realisation ratios, the December quarter survey implies that total capex is expected to drop by over 10% in 2014/15, driven by a 17% decline in mining investment, following a more than 5% fall in 2013/14.

Capital survey year-ahead expectations and actuals



* Estimate 1: 12 months expectation as reported in Jan-Feb survey of previous financial year
** First 6 months are actuals, second 6 months are expectations from estimate 5
Source: ABS

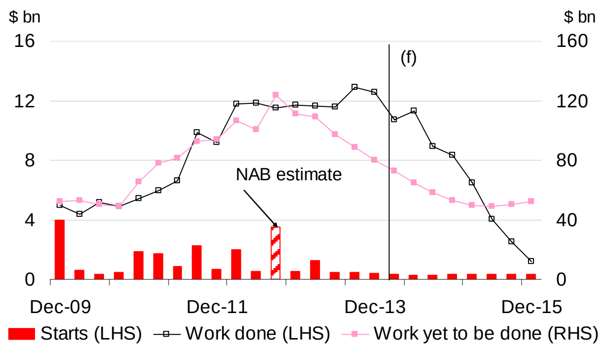
Engineering construction work yet to be done



Source: ABS

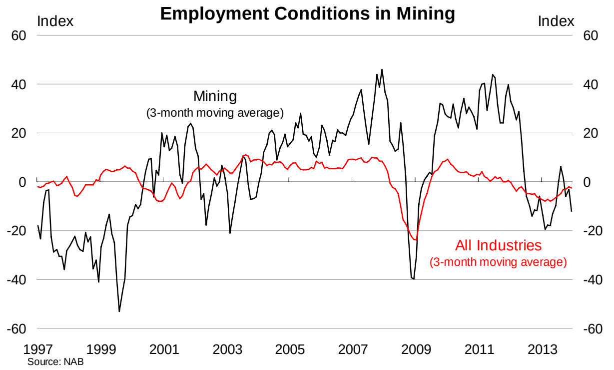
Rates of mining investment 'work done' slowed in the December quarter, but not enough to offset the limited number of new projects commenced. Consequently, the pipeline of mining investment yet to be done diminished, falling from almost 2½ years of construction at the end of 2012 to a little over 1½ years by the end of 2013 (a ratio of work-yet-to-be-done to work-done). The pipeline is expected to level out over 2015 once investment activity slows considerably. Consistent with the shifting phase of the mining boom (lower prices and construction activity), business conditions reported by mining firms in NAB's monthly business survey have been soft – underperforming all other industries in the latest April survey. On the flip side, the mining sector will contribute to national output through strengthening net export volumes, which are expected to gain momentum over the next two years as major resource projects (particularly LNG) begin to deliver. Overall, we expect exports to grow by around 6¾% in 2013/14, and around 9½% in 2014/15. With the AUD expected to soften modestly over the forecast horizon, along with capital imports, we expect total imports to contract – with growth of -4% in 2013/14 and -½% in 2014/15.

Mining engineering construction



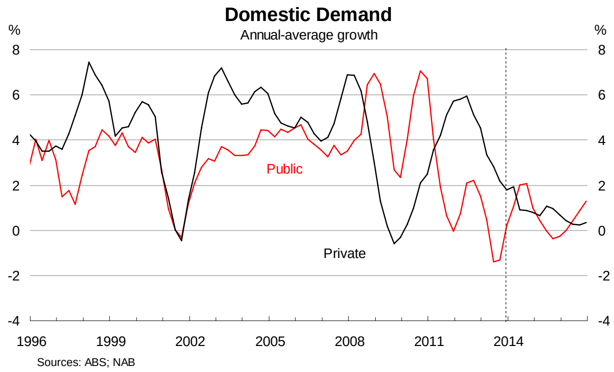
Sources: ABS, NAB estimates

In addition to the direct drag on business investment, the decline in mining investment is expected to have a significant impact on the labour market – with flow on effects to the rest of the economy. This is because the resource boom is shifting from labour intensive investment to the capital intensive exports phase. Mining employment demand is already being reduced as a consequence. The impact on the labour market is likely to be partly offset by improving labour demand in sectors such as residential construction in the near term and engineering construction in the medium to longer-term (reflecting the government infrastructure investment program which is expected to yield around 30,000 new jobs in the long-run), although public sector job cuts will also be large. Frictional unemployment will still see the unemployment rate lift further.

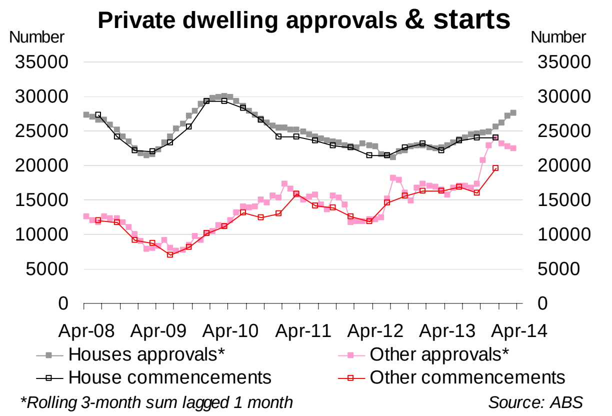


Currently, official data show that labour market conditions have started to improve following a steady deterioration over the past 12-months. Improvements in pockets of the economy have seen employment start to grow again, while a falling participation rate has also helped the unemployment rate ease to 5.8%, from a peak of 6% early in the year. Looking at the near-term, there appears to be some scope for further improvements with leading indicators such as job vacancies lifting from recent lows.

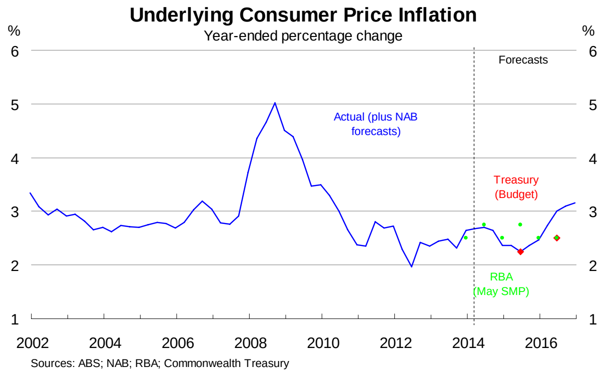
While slack in the labour market and higher anxiety over job security will keep income growth subdued and households cautious about their spending and borrowing decisions, low borrowing rates and rising asset prices have provided some impetus to consumption since late last year. However, some of the steam has been lost more recently. Consumer confidence has fallen dramatically in response to a number of factors, including uncertainty over potential negative impacts from the Federal Budget, offsetting support from low interest rates and higher asset prices. While 'green shoots' appear to be emerging in the consumer dependent sectors, the NAB business survey shows that conditions in these industries – retail, wholesale etc – are still challenging. We see private consumption growth of around 2¾% in 2013/14, before lifting to around 3¼ in 2014/15.



Borrowing rates have been at historically low levels and are expected to stay low for a while to come. They have contributed to strengthening property markets, helping to offset headwinds from the deteriorating labour market. Higher property prices and strong demand (particularly from investors) triggered a strong rise in dwelling approvals, which will contribute to a notable rise in dwelling investment over the course of the year. However, both the rise in supply and the lingering slack in the labour market will likely limit additional price rises and weigh on dwelling investment further along the forecast horizon; NAB's consumer anxiety survey shows growing anxiety over job security. Overall, we expect dwellings investment to rise by around 4¼% in 2013/14, before rising by around 9% in 2014/15.



Despite a blow-out in the Government's underlying cash balance to an estimated $49.9 billion in 2013/14, from $18.8 billion in 2012/13 (and an expected deficit of $18 billion at the time of the last budget), spending cuts kept public demand broadly flat in 2013. This trend towards 'fiscal austerity' is expected to continue over coming years as the government pursues its medium-term objective of obtaining a 1% of GDP surplus. Treasury expects underlying public final demand growth to be around 1¾% in 2013/14 and slightly softer at 1½% in 2014/15 – a little stronger than NAB's forecast.



Based on the offsetting factors facing the economy, our assessment is that the RBA is unlikely to undertake any additional monetary easing in the current cycle, even as the unemployment rate lifts a little further. Limited wage pressures and a stubbornly elevated AUD will keep underlying inflation comfortably within the RBA's target band, although strength in dwelling prices is certainly a concern. At the same time, the RBA expect the unemployment rate to peak in the near-term, in line with improvements in timely indicators of economic activity. With that said, the RBA is also reluctant to commence tightening rates for fear of stifling the recovery in interest sensitive sectors of the economy and will likely keep rates at current levels until at least late 2015. There are, however, still significant uncertainties. A larger than expected drag from the mining sector being the most likely.

Australian Economic and Financial Forecasts – National v Federal Budget (a)

End Period	**2013-14 (f)**		**2014-15 (f)**	
Annual % Change	**NAB**	**Budget**	**NAB**	**Budget**
Private Consumption	2.8	2½	3.3	3
Private Investment – Dwelling	4.2	3½	9.1	7½
Underlying Business Fixed Investment	-7.0	-4	-11.1	-5½
Underlying Public Final Demand	2.0	1¾	0.0	1½
Domestic Demand	**1.4**	**1½**	**0.8**	**1½**
Stocks – Contribution to GDP	-0.4	-¼	0.1	0
GNE	**1.0**	**1¼**	**0.9**	**1¾**
Exports	13.4	5½	13.1	5½
Imports	4.9	-3	6.1	2
GDP	**2.9**	**2¾**	**3.1**	**2½**
- Non-Farm GDP	2.8	**2¾**	3.1	2½
- Farm GDP	6.5	5	2.1	-4
Federal Budget Deficit (fiscal balance, $bn)	**-45.1**	**-45.1**	**-25.9**	**-25.9**
Current Account Deficit: % of GDP (-%)	-2.1	-3¼	-0.5	-4
Terms of Trade	-2.7	-5	-2.9	-6¾
World GDP (b)	3½	3½	3.7	3¾
End Period				
Wage Price Index	2.9	2¾	3.3	3
Employment	1.0	¾	1.8	1½
Unemployment rate	6.1	6	6.1	6¼
Underlying CPI	2.7	n.a.	2.3	2¼
Official Cash Rate	2.50	n.a	2.50	n.a.
10 Year Govt. Bond Yield	3.95	n.a	4.60	n.a.
US cents/$A	0.87	n.a	0.82	n.a.
Trade Weighted Index	69.7	n.a	67.9	n.a.

(a) Percentage change on previous year, unless otherwise indicated (b) Calendar (f) Forecast

Forecast Comparisons

GDP	**Dec 2012**	**Jun 2013**	**Dec 2013**	**Jun 2014**	**Dec 2014**	**Jun 2015**
NAB	2.4	2.9	3.3	3.1	2.8	2.7
RBA	2.40	2¾	3.00	2¼-3¼	2¼-3¼	2½-4
Treasury		2¾		2½		3
CORE INFLATION*						
NAB	2.6	2.7	2.4	2.3	2.5	3.0
RBA	2½	2¾	2½	2¼-3¼	2-3	2-3
Treasury				2¼		2½

(a) Year-average percentage change
(b) Year-ended percentage change

Bond Issuance and Net Debt

The Debt Program in 2014/15.

In line with continued deficits, the Government will continue to be net issuer of Commonwealth Government stock (CGS) in the years ahead, albeit it at a slow pace.

Even so, the Budget projects the face value of CGS peaking at $470bn in 2017-18, from around $330bn at the June 2014. As a share of GDP, CGS issuance is to peak at 25%, which remains quite modest from a global perspective.

In the out-years (2018/19 and beyond) CGS outstandings are expected to fall as the Budget returns to surplus.

Net debt – including the likes of the Future Funds assets – is now expected to peak around 14-15% of GDP

2014/15 Debt Program

AOFM (Australian Office of Financial Management – the Government's debt management arm) will give more detail on their 2013/14 programme in the days ahead.

But the broad parameters are that CGS issuance is expected to be a net $40bn in 2014/15, less than the net $63bn of issuance expected for the year to June 2014.

Issuance through 2013/14 was predominately the benchmark ACGB program with a mix of index linked issuance and t-notes where needed. This pattern is likely to be repeated in 2014/15.

So accounting for 27bn of ACGB maturities in 2014/15, this would imply gross ACGB issuance of between $60-65bn.

Rating Agencies Comfortable with Australia strong AAA rating:

S&P comments according to Bloomberg

- *Australia's stable AAA rating not immediately affected by the government's budget for the year through June 2015*
- *Budget projections broadly in line with expectations, S&P says*
- *Sees budget performance gradually improving over medium term*
- *Sees general government debt burden remaining low*
- *Budget is consistent with S&P's view of strong political commitment to prudent.,*

Moody's analyst Steven Hess comments

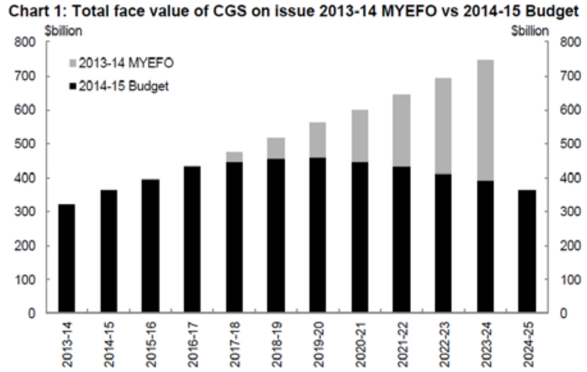
- *Budget is "definitely credit positive," he says*
- *Measures have improved fiscal outlook "quite significantly"*
- *Forecast peak for Australia net debt "quite low"*
- *Australia's AAA rating supported by low level of debt*
- *GDP growth outlook still "fairly good"*
- *"This is a good start at facing the pressures coming from social programs on government spending,"*
- *Australian budget package looks credible overall, according to Hess*

Debt and CGS Statistics

	2012/13	2013/14	2014/15	2015/16
Net Debt				
- $bn	153.0	197.9	226.4	246.4
- % GDP	10	12.5	13.9	14.4
Gross Debt				
- $bn	153.0	197.9	226.4	246.4
- % GDP	10	12.5	13.9	14.4
CGS - Face Value				
- $bn	257	320	360	390
- % GDP	16.7	20.2	22.1	22.8
Of which				
ACGB	234	298*		
Linker	18	22*		
T Bills	6			
	258	320	360	390

* estimate

Chart 1: Total face value of CGS on issue 2013-14 MYEFO vs 2014-15 Budget



Note: A tax-to-GDP cap of 23.9 per cent has been applied to these projections. This is the average tax-to-GDP ratio in the years post-GST and pre-GFC. MYEFO tax-cap projection was not published at MYEFO.
Source: Australian Office of Financial Management and Treasury projections.

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