



AUSTRALIAN BUDGET 2019-20

No big cash splash: Government focuses on economic management credentials, provides modest further immediate income tax relief for low/middle income earners and adds to its large infrastructure plans over the next decade.

HOW TO ASSESS THE BUDGET – *as always, there are competing priorities!*

- **Short-term forecasts**

- Are the fiscal and economic assumptions credible?
- Do they secure Australia's AAA rating?

- **Long-term fiscal sustainability**

- Does the Budget help rebuild fiscal flexibility?
- Does the Budget address the long-term fiscal challenges of the ageing population?
- Is the level of expenditure correct and appropriately targeted? Are the various agents paying appropriate tax?

- **Policy Initiatives and the Economy**

- Does the Budget support productivity and jobs growth?
- Are the economy's/government's resources being used appropriately – is sufficient infrastructure provided for?

- **Fairness**

- Does the Budget support Australian's sense of a fair go – rewarding initiative as well as providing a social safety net?

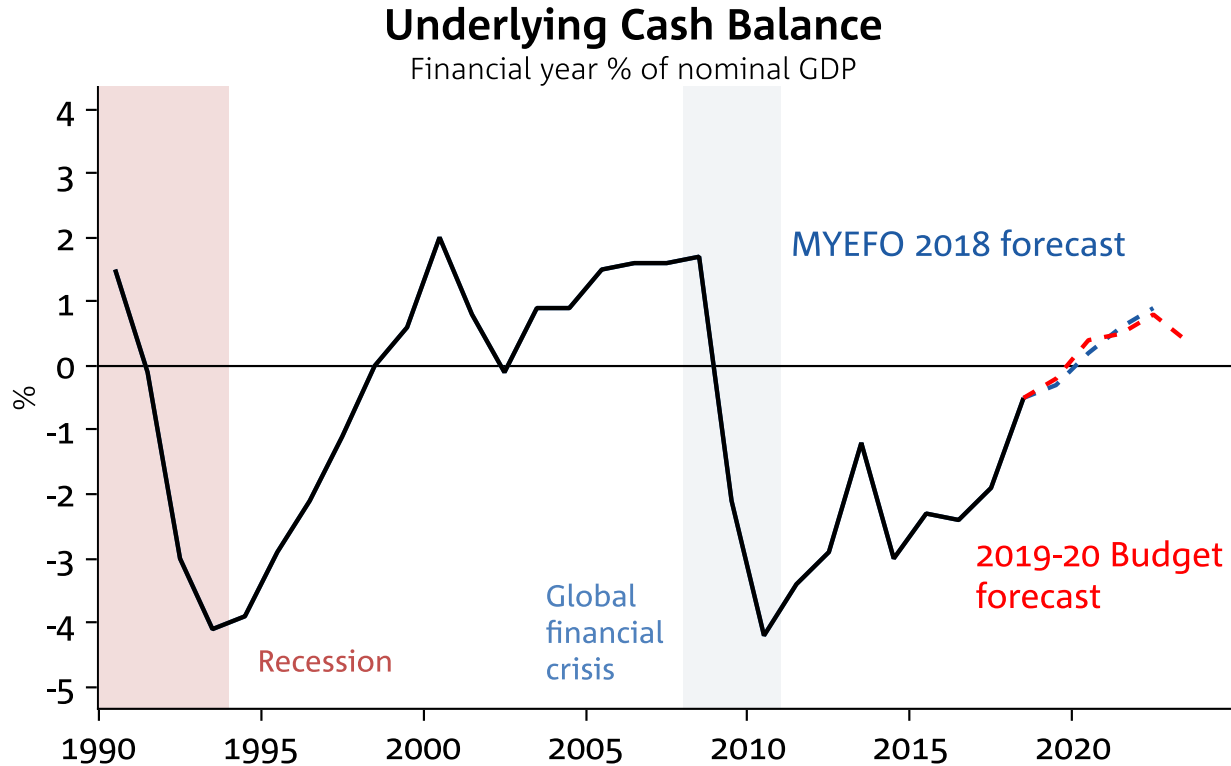
- **Politics**

- Will it help the Government get re-elected?

- **What's not in the Budget?**

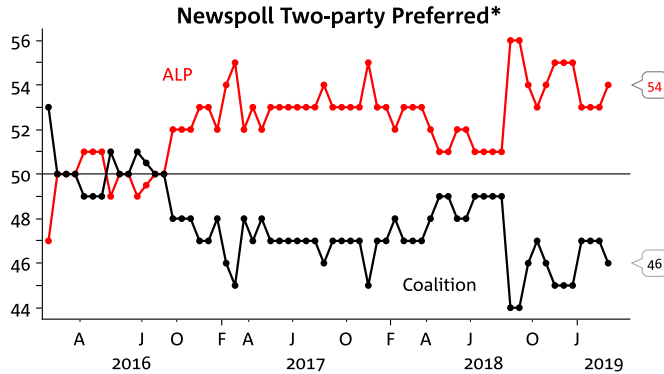
- Are key economic issues addressed – eg. housing affordability, energy security, education, retirement savings, immigration, tax rates, climate change etc.?

THE GOOD NEWS – *should return to surplus this financial year!*

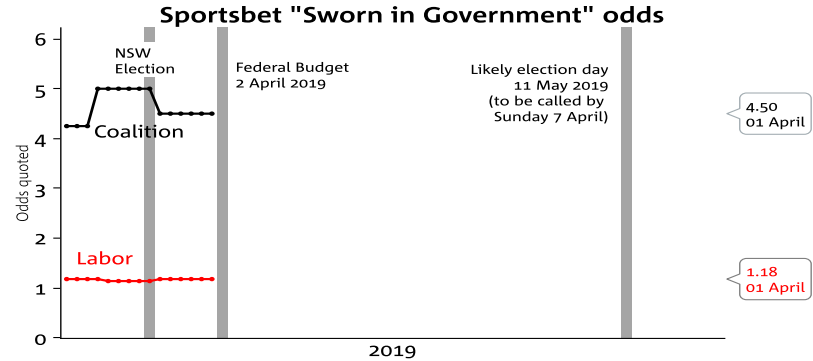


Source: National Australia Bank, Treasury

A CAMPAIGN BUDGET



* Based on preference flows at the Jul 2016 election, adjusted for minor party preference flows, including One Nation since Dec 2017
Source: National Australia Bank, Newspoll



* Odds quoted for "Sworn in Government".
Source: National Australia Bank, Sportsbet

KEY MEASURES – no big cash splash, more immediate income tax relief for low/middle income earners

Main revenue/savings measures

- **Personal income tax cuts/Medicare levy threshold for low-income earners:** Low and middle income tax offset more than doubled (flows from 1 July). Large cuts only from 2024-25 (30% tax rate for 90% of taxpayers). Small cost (only \$6.0b over 4 years as money was already set aside in last year's Budget update and most outside the forecast period).
- **Crackdown on tax avoidance by large corporates, multinationals and wealthy individuals** (raises \$3.6b over 4 years)
- **Reduce overpayment to welfare recipients:** reduce overpayments by automating the reporting of wages earned by welfare recipients (raises \$2.1b over 4 years)

Main spending measures

- **Infrastructure:** mainly spending on roads (costs \$4.5b over 4 years) – 10-year plan increased to \$100bn from \$75bn
- **Primary health care:** spending mainly on chronic disease care and general practice (costs \$1.0b over 5 years)
- **Aged care:** focus on quality, safety and accessibility of residential and home care services (costs \$0.7b over 5 years)

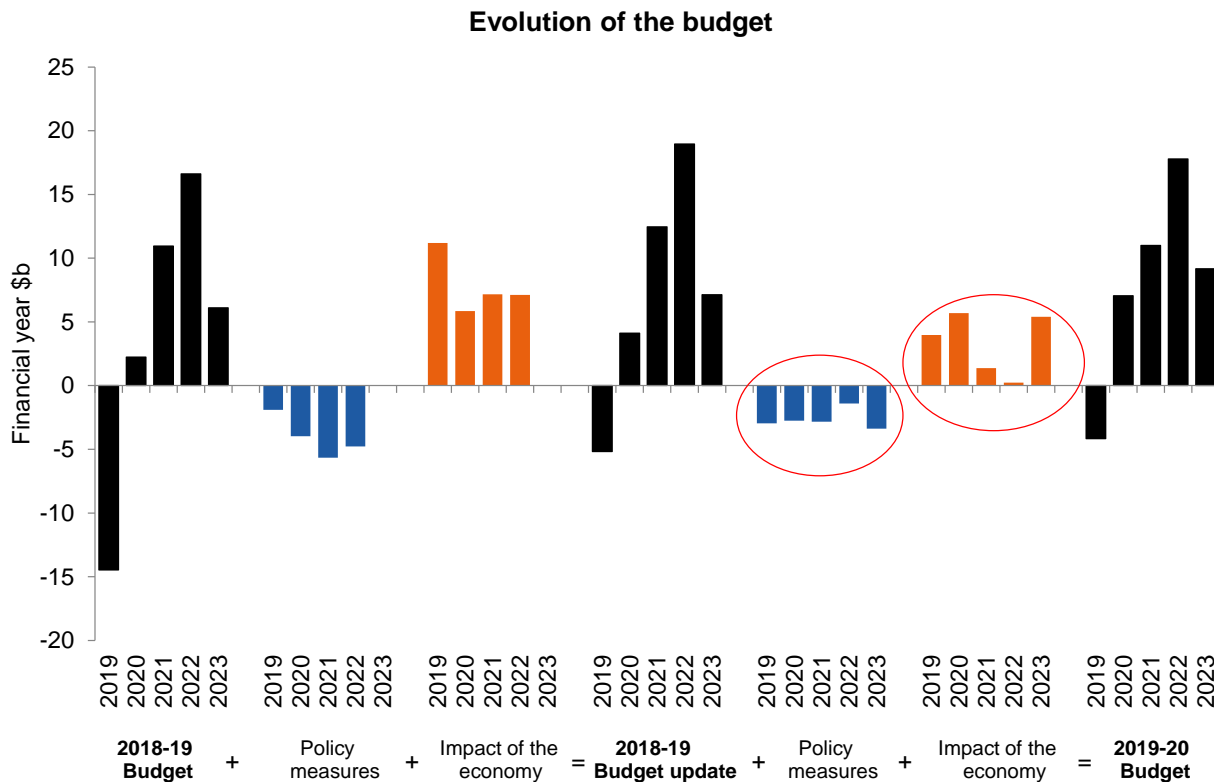
KEY FIGURES – forecast return to surplus in 2019-20, building to over 1% of GDP surpluses in the medium term

Table 1: Key Budget Aggregates 2019-20

	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
	Actual		Forecasts			
Underlying cash balance	-10.1	-4.2	7.1	11.0	17.8	9.2
<i>(% of GDP)</i>	<i>(-0.5)</i>	<i>(-0.2)</i>	<i>(0.4)</i>	<i>(0.5)</i>	<i>(0.8)</i>	<i>(0.4)</i>
MYEFO December 2018		-5.2	4.1	12.5	19	
Budget 2018-19		-14.5	2.2	11	16.6	
Headline cash balance	-25.9	-12.7	-4.4	-0.5	7.9	2.5
<i>(% of GDP)</i>	<i>(-1.4)</i>	<i>(-0.7)</i>	<i>(-0.2)</i>	<i>(0.0)</i>	<i>(0.4)</i>	<i>(0.1)</i>
MYEFO December 2018		-18.3	-7.2	2	4.5	
Budget 2018-19		-27.6	-8.1	21	7.8	
Gross debt	531.9	546.0	560.0	567.0	573.0	569.0
<i>(% of GDP)</i>	<i>(28.8)</i>	<i>(28.1)</i>	<i>(27.9)</i>	<i>(27.3)</i>	<i>(26.4)</i>	<i>(25.0)</i>
MYEFO December 2018	531.0	542.0	558.0	563.0	567.0	
Budget 2018-19	540.0	561.0	578.0	566.0	578.0	

Source: National Australia Bank, Treasury

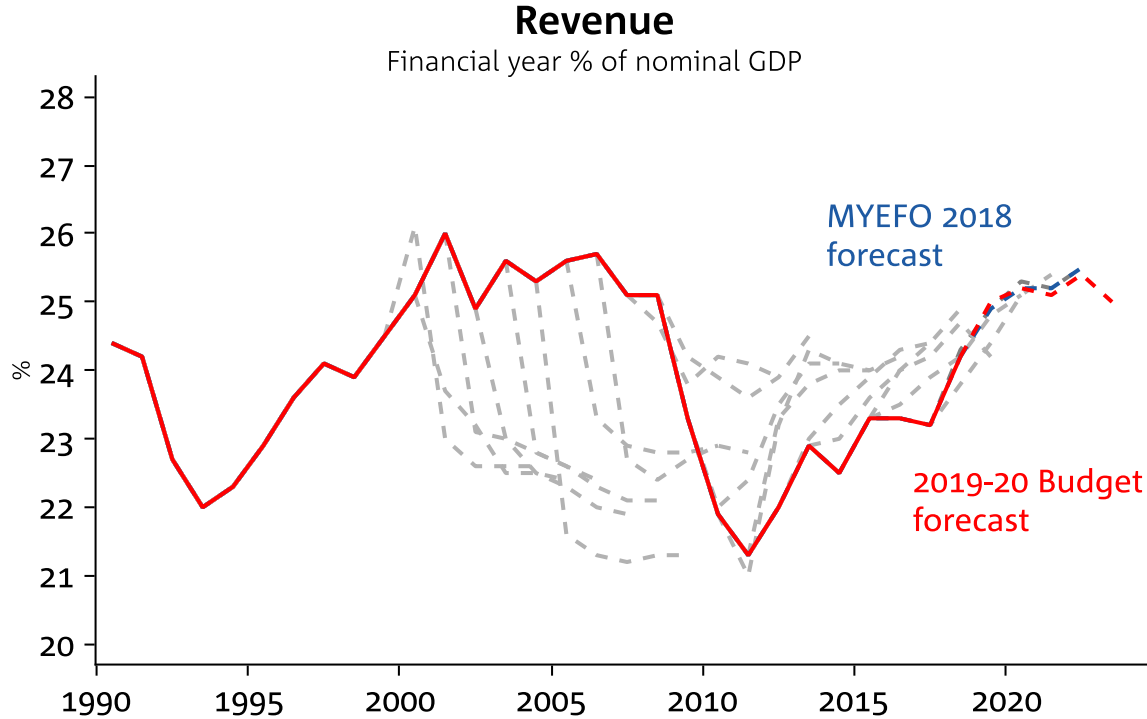
HOW DID WE GET HERE? – improvement driven by economy allows very modest policy measures while still maintaining budget improvement



Source: Treasury, National Australia Bank

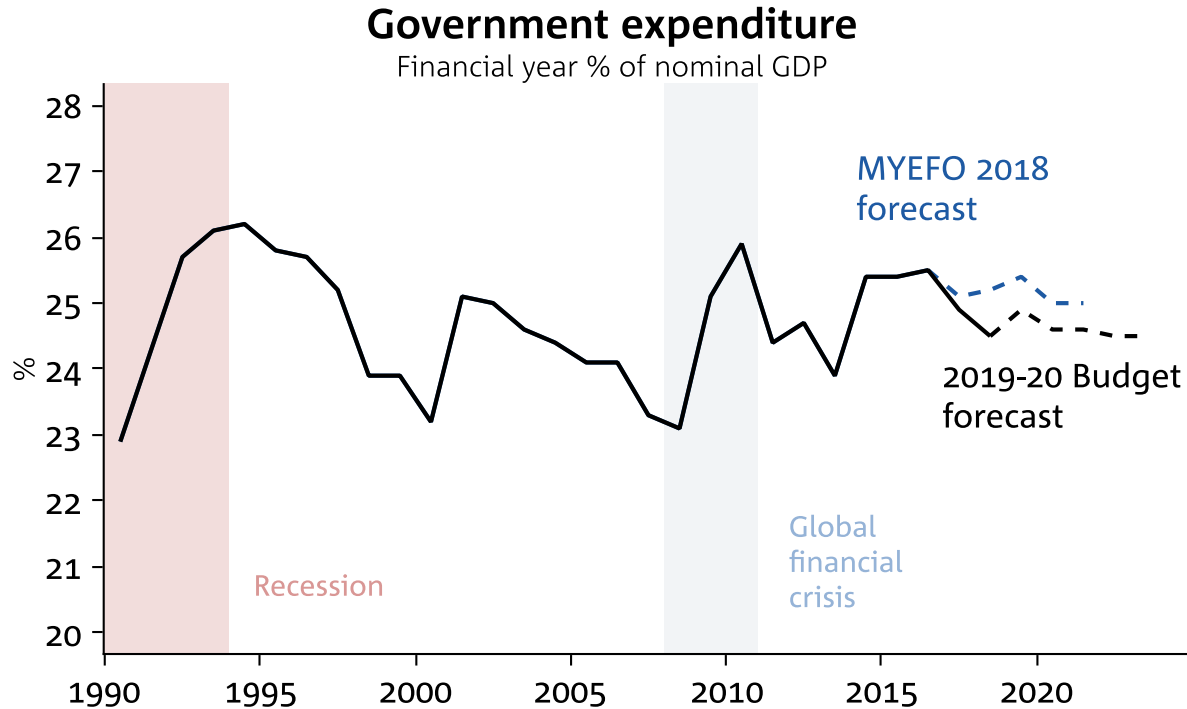


BUDGET REVENUE – stronger revenue given high commodity prices and solid jobs growth



Source: National Australia Bank, Macrobond

BUDGET SPENDING – spending has been kept under control, especially welfare



Note: Cash receipts cover consumption, investment, grants and welfare payments.

Source: National Australia Bank, Treasury

ECONOMIC FORECASTS – appropriately conservative on terms of trade; possibly somewhat optimistic on growth, inflation and wages pick-up

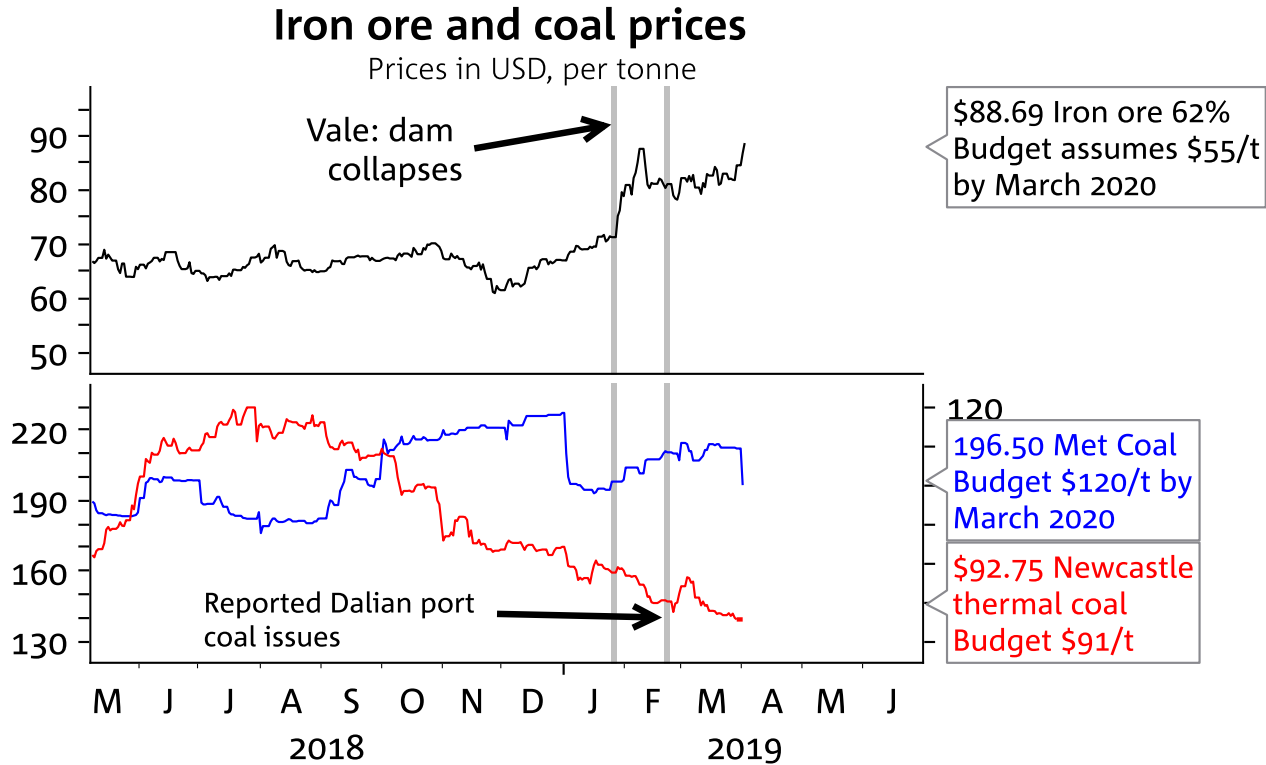
Key Economic Forecasts (a)	2019-20 Budget						NAB	
	Outcome		Forecasts				Forecasts	
	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2018-19	2019-20
Real GDP	2.8	2.25	2.75	2.75	3	3	2.2	2.3
Employment (b)	2.7	2	1.75	1.75	1½	1½	2.3	1.3
Unemployment Rate (b)	5.4	5	5	5	5	5	5.1	5.1
Inflation (CPI) (b)	2.1	1.5	2.25	2.5	2½	2½	1.8	2.6
Wages (WPI) (b)	2.1	2.5	2.75	3.25	3½	3½	2.3	2.7
Compensation of employees	4.5	4.25	4.25	4.75	5	5	n/a	n/a
Terms of trade	1.9	4	-5.25	-4.75	n/a	n/a	1.4	-3.3
Nominal GDP	4.7	5	3.25	3.75	4.5	4.5	3.9	4.4

(a) Year-average growth unless otherwise stated.

(b) Year-ended growth to the June quarter; unemployment rate June quarter average.

Source: ABS, Treasury, NAB

IRON ORE ASSUMED TO GET TO \$55 BY MARCH '20, MET COAL TO \$120

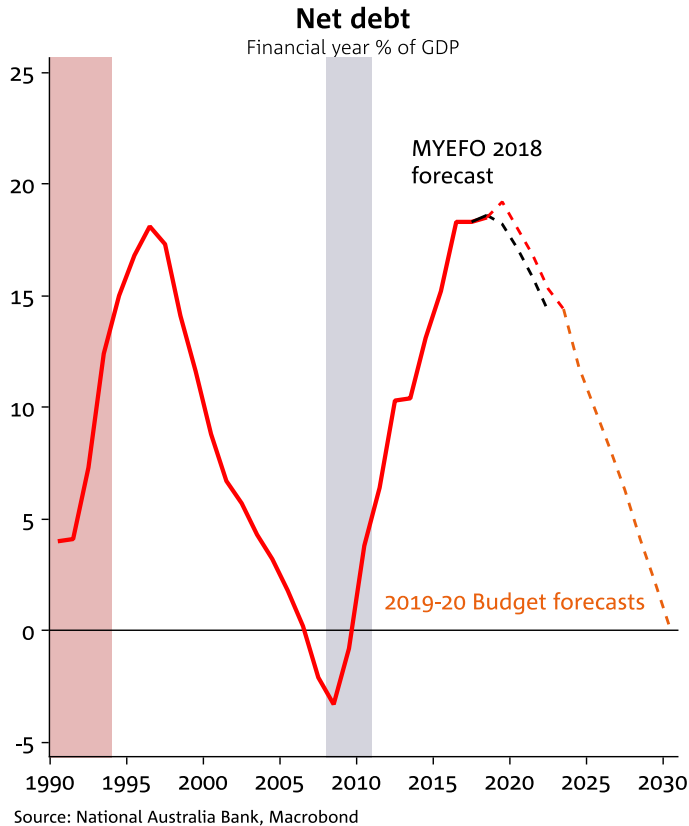


Source: National Australia Bank, Macrobond

RISKS – *what can go wrong?*

- **World economic slowdown:** Global outlook is more uncertain though the Federal Reserve is now on the sidelines after raising rates over recent years
- **US-China trade tensions:** There has been a shift to increased protectionism with the US and China yet to agree on trade, though markets remain optimistic
- **China slowdown and commodity prices:** China's growth slows too much as authorities try to reduce the economy's heavy debt load. Budget assumes lower commodity prices which is sensible
- **Housing market correction:** Falling house prices and falling construction could have greater spill over to the rest of the economy than currently expected

AAA CREDIT RATING – Australia retained its AAA rating last year



- Moody's – Aaa stable

- “Australia’s general government debt to GDP is still pretty much in line with AAA-rated peers ... there are some downside risks to the revenue outlook”.

KEY CAMPAIGN POLICIES

Coalition policies:

- Its economic track record
- Income tax cuts
- Reducing the cost-of-living (especially health access and energy prices)
- Infrastructure (especially regions) and Immigration

Labor policies:

- Increasing the disposable income of low/middle-income workers, including the living wage
- Reducing the cost of living (especially health and energy prices)
- Tackling climate change / greener energy
- Boosting health and education spending
- Reforms to “high income” tax concessions (negative gearing, franking credit refunds, trusts)
- ‘Bigger, better’ budget surplus

Labor's Fair Go Action Plan

- ✓ Fix our schools and hospitals.
- ✓ Ease pressure on family budgets.
- ✓ Stand up for workers.
- ✓ Invest in cheaper, cleaner energy.
- ✓ Build a strong economy that works for us all.

the next election will be a referendum on wages.

It will be a contest about who the economy should work for, whose interests the system should serve.

LABOR'S PLAN FOR HEALTH

1. We will end Malcolm Turnbull's freeze on Medicare.
2. We will properly fund our hospitals.
3. We will cap out of control private health premium increases.

ONLY LABOR WILL FULLY FUND PUBLIC SCHOOLS

LABOR WILL DELIVER:

- FUNDING FOR EXTRA TEACHERS AND RESOURCES
- MORE INDIVIDUAL ATTENTION FOR STUDENTS
- EXTRA SUPPORT FOR KIDS WITH SPECIAL NEEDS

A FAIR GO FOR AUSTRALIA

FAIRGOACTIONPLAN.ORG.AU

More than 3.9 million Australians will receive a one-off Energy Assistance Payment to help with their next energy bill.

LIBERAL BACKING SMALL BUSINESS
\$2 BILLION FUND TO SUPPORT GROWTH

PLANNING FOR AUSTRALIA'S FUTURE POPULATION:

- ✓ REDUCE THE MIGRATION CAP
- ✓ FIX CONGESTION
- ✓ PLAN FOR THE FUTURE

CLIMATE SOLUTIONS FUND
\$2 billion to reduce carbon emissions

PERSONAL TAX CUTS – immediate doubling of LMITO (flows from 1 July); 30% tax rate introduced for \$45-200K from 1 July 2024 (previously 32.5%)

Last year's budget

Table 3: New personal tax rates and thresholds 2018–19, 2022–23 and 2024–25

Rate (%)	Current tax thresholds Income range (\$)	New tax thresholds From 1 July 2018 Income range (\$)	New tax thresholds From 1 July 2022 Income range (\$)	New tax thresholds From 1 July 2024 Income range (\$)
Tax free	0 - 18,200	0 - 18,200	0 - 18,200	0 - 18,200
19	18,201 - 37,000	18,201 - 37,000	18,201 - 41,000	18,201 - 41,000
32.5	37,001 - 87,000	37,001 - 90,000	41,001 - 120,000	41,001 - 200,000
37	87,001 - 180,000	90,001 - 180,000	120,001 - 180,000	-
45	>180,000	>180,000	>180,000	>200,000
Low and middle income tax offset	-	Up to 530	-	-
LITO	Up to 445	Up to 445	Up to 645	Up to 645

This year:

Table 3: New personal tax rates and thresholds

Rate (%)	2017-18 tax thresholds Income range (\$)	Current tax thresholds From 1 July 2018 Income range (\$)	New tax thresholds From 1 July 2018 Income range (\$)	New tax thresholds From 1 July 2022 Income range (\$)	Rate (%) From 1 July 2024	New tax thresholds From 1 July 2024 Income range (\$)
Tax free	0 - 18,200	0 - 18,200	0 - 18,200	0 - 18,200	Tax free	0 - 18,200
19	18,201 - 37,000	18,201 - 37,000	18,201 - 37,000	18,201 - 45,000	19	18,201 - 45,000
32.5	37,001 - 87,000	37,001 - 90,000	37,001 - 90,000	45,001 - 120,000	30	45,001 - 200,000
37	87,001 - 180,000	90,001 - 180,000	90,001 - 180,000	120,001 - 180,000	45	>200,000
45	>180,000	>180,000	>180,000	>180,000	LITO	Up to 700
Low and middle income tax offset	-	Up to 530	Up to 1,080	-		
LITO	Up to 445	Up to 445	Up to 445	Up to 700		

NEW INFRASTRUCTURE SPENDING – *key projects*

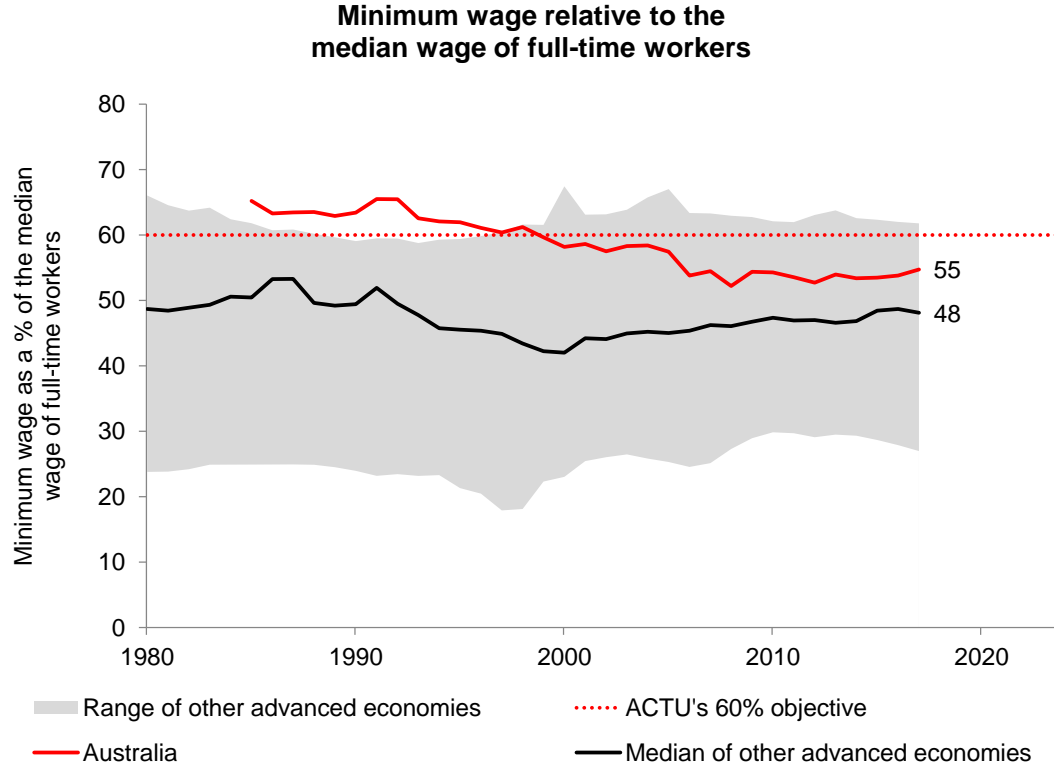
The government plans to increase infrastructure spending from \$75b to \$100b over the next ten years. While a large number, this is around 0.4% of GDP over this period.

Some of the bigger new projects include:

- **VIC** \$2b for fast rail from Geelong to Melbourne
- **SA** North-South Corridor, \$1.5b
- **NSW** Western Sydney Rail, \$3.5b
- **NSW** M1 Pacific Highway Extension, \$1.6b
- **VIC** Suburban Roads upgrades, \$1.1b
- **QLD** Gateway Motorway, \$800m
- **WA** Tonkin Highway, \$349m

THE LIVING WAGE

Labor plans to change the minimum wage to facilitate a living wage (60% of median wage). This would require an 11.5% increase over two years – but likely to be phased in over longer period



Source: OECD, National Australia Bank

WHAT'S NOT IN THE BUDGET?

- **Broader reform of the tax system:** Changing the mix of taxation to increase the GST and reduce corporate tax. Tax relief for top income earners (politically difficult – something for the next term?)
- **Reform of federal/state financial relations:** Recent Commonwealth payments to Western Australia are outside the scope of the traditional framework for supporting the states
- **Reform of the housing market:** There are no long-term measures to address housing affordability in partnership with state government
- **Climate change:** Labor leads the Government on this policy
- **Company tax cuts and income tax cuts for high-income earners:** not politically deliverable

MARKING THE BUDGET

- **Short term forecasts**

- Fiscal and economic assumptions are mostly credible in the short term (maybe slightly optimistic, though growth will be supported by tax cuts) ✓

- **Long term fiscal sustainability**

- Continued focus in this budget on rebuilding fiscal flexibility and paying down debt – no big cash splash ✓

- **Policy Initiatives and the Economy**

- Income tax cuts supportive of the economy in the short term
- Infrastructure spending supportive of economy and productivity, in the longer term ✓
- Absence of other medium-term policies (see what's not in the budget)

- **Fairness**

- Does the Budget support Australian's sense of a fair go – rewarding initiative as well as providing a social safety net? ✓

- **Politics**

- Will it help the Government get re-elected? ?

- **What's not in the Budget?**

- Arguably still not enough consideration of major tax reform, reform of Federation, climate change – still very high top marginal tax rate and relatively high company tax rate X

ECONOMIC OUTLOOK

THINKING ABOUT THE AUSTRALIAN ECONOMIC CYCLE – *Sector rotation at a macro level: housing downturn and slower overall growth, but so far no economy-wide downturn*

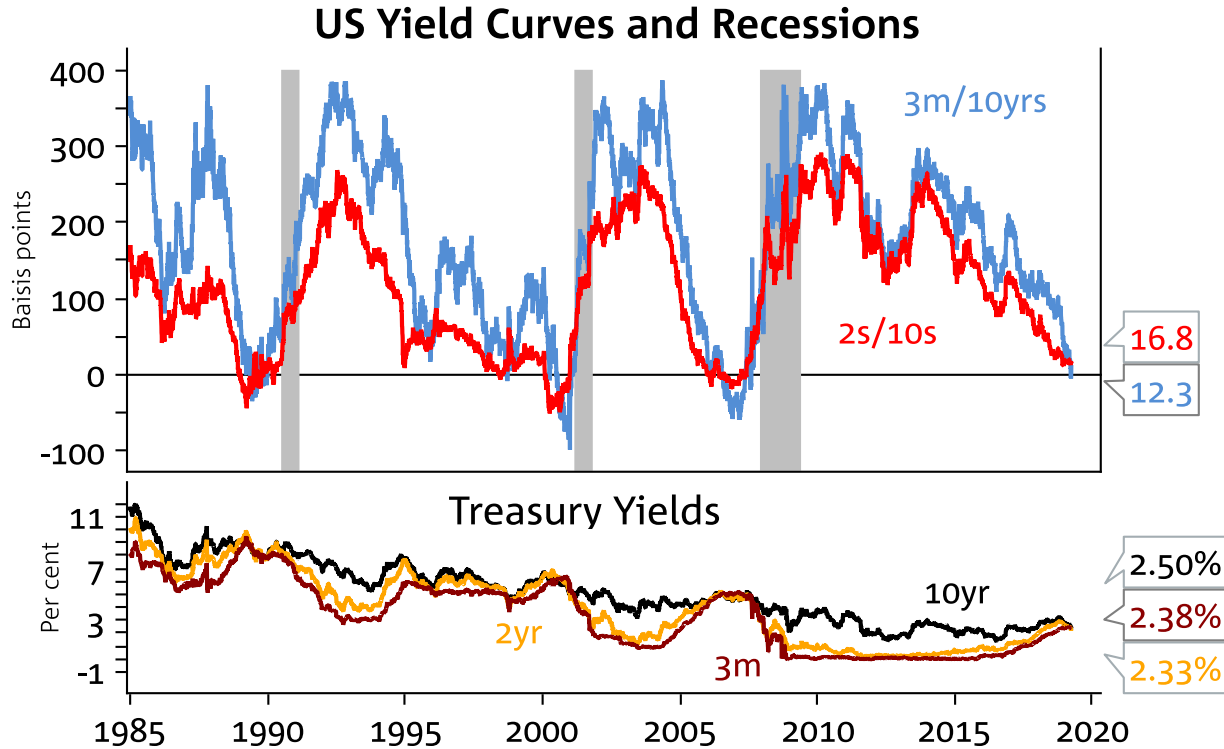
Forces/factors **restraining/easing** economic growth:

- Housing downturn (prices, construction, lending standard, wealth)
- Spill overs from housing turnover and construction into retail, manufacturing and transport
- Drought (temporary – severe on East Coast, but great crop in the West)
- Interest rates (modest rises to date; recent easing in pressure on funding costs)
- Global growth – Europe/China/manufacturing/geopolitics
- Australian politics

Forces/factors **supporting** economic growth:

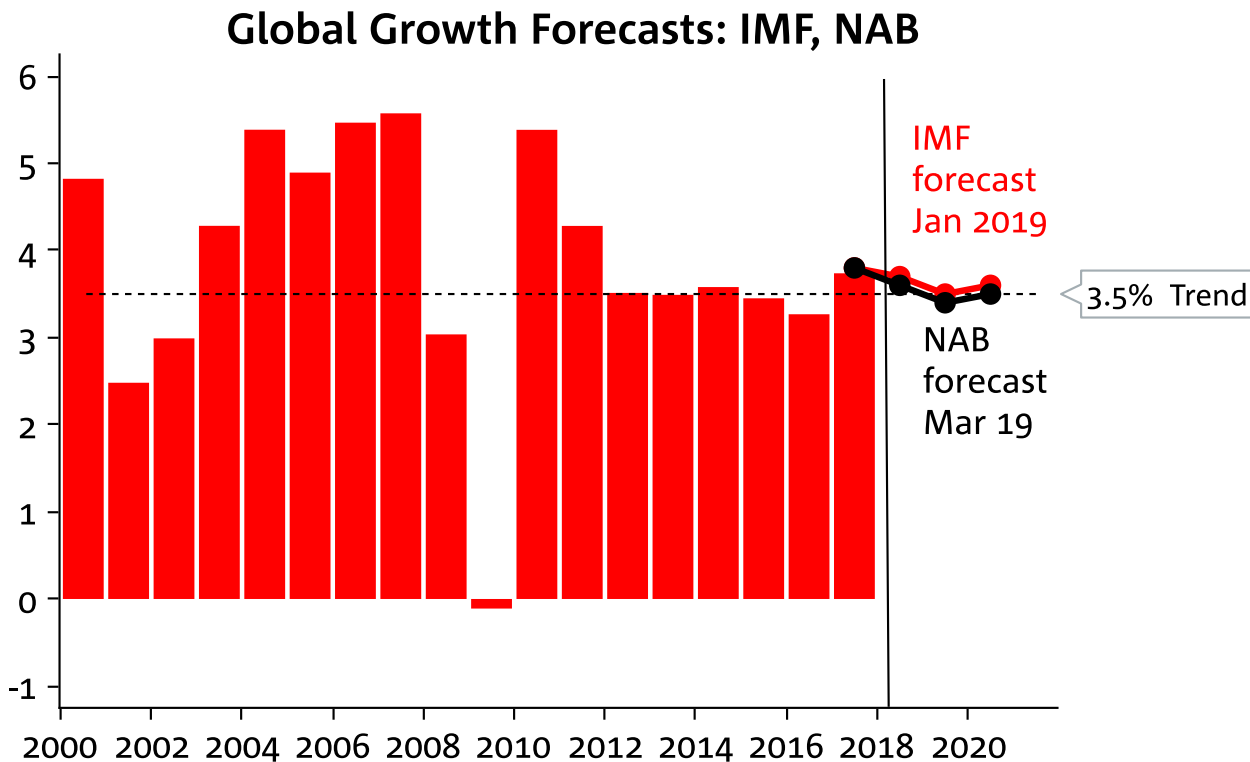
- Infrastructure spending
- Defence spending
- End of mining downturn/mining investment recovery (from headwind to tailwind)
- Non-mining investment recovery
- Commodity prices (oil/base metals a bit lower recently, but iron ore and coal holding up well)
- Lower \$A
- Fiscal easing/income tax cuts (latter don't begin until July 2019; more to be announced on April 2nd?)
- Employment/low unemployment & beginnings of improvement in wages growth
- Population (a bit slower than in previous years – follow immigration debate)

GLOBAL GROWTH – flattening of US yield curve has caused concern about possible recession



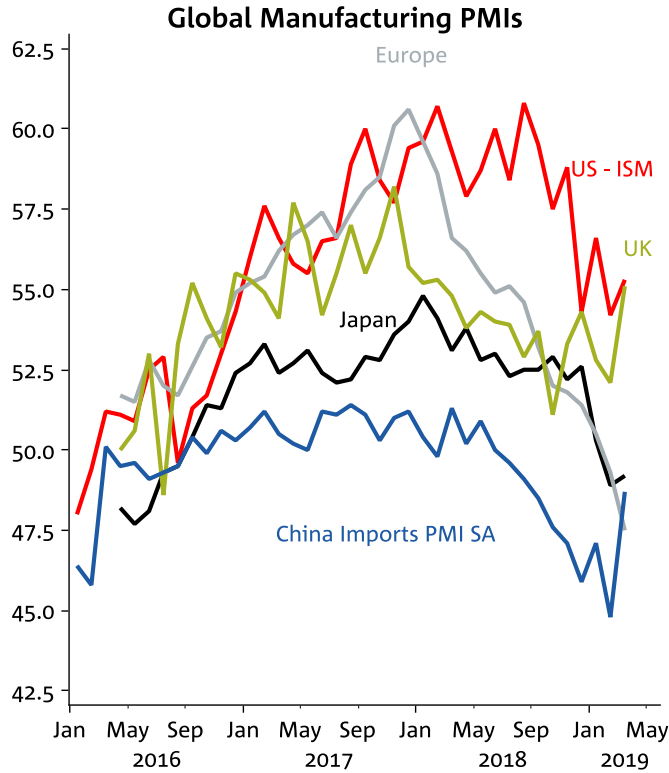
Source: National Australia Bank, Bloomberg

GLOBAL GROWTH – forecasts have been downgraded but still broadly around trend. Central banks worrying about downside risks.

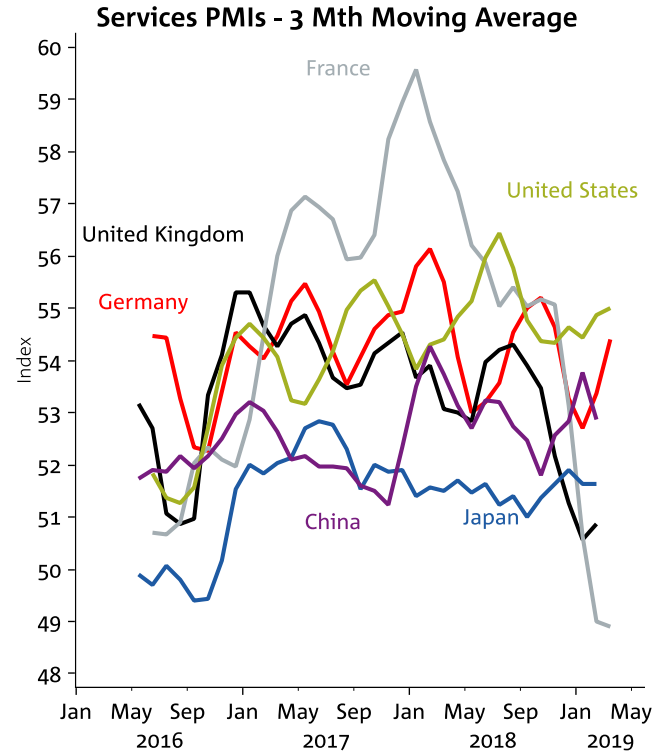


Source: National Australia Bank, IMF, Macrobond.

GLOBAL GROWTH – slowing has been centred in manufacturing (China/US trade war, Brexit, Fed tightening); services more robust

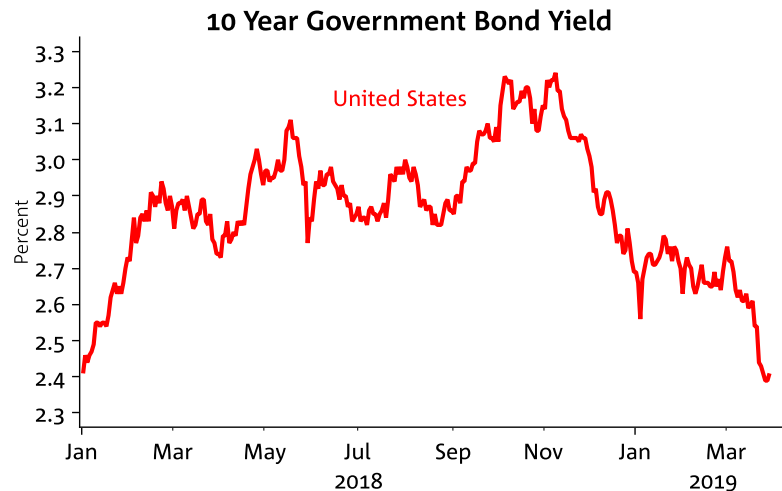
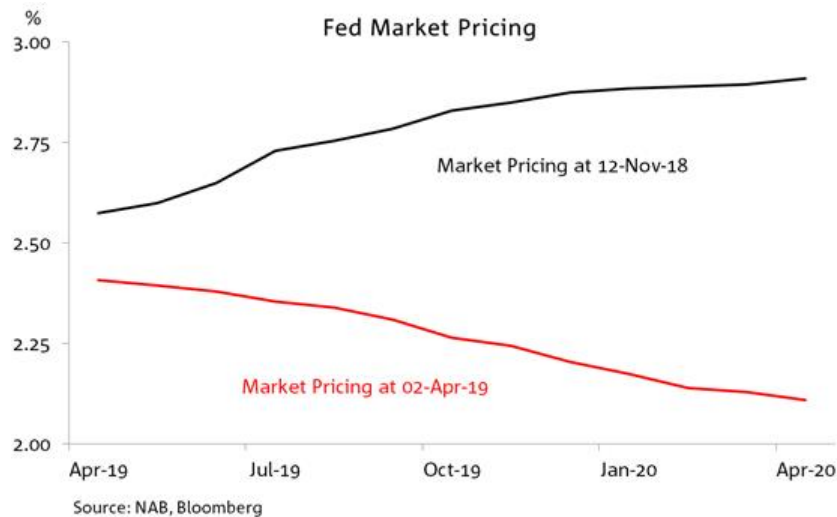


Source: National Australia Bank, Macrobond

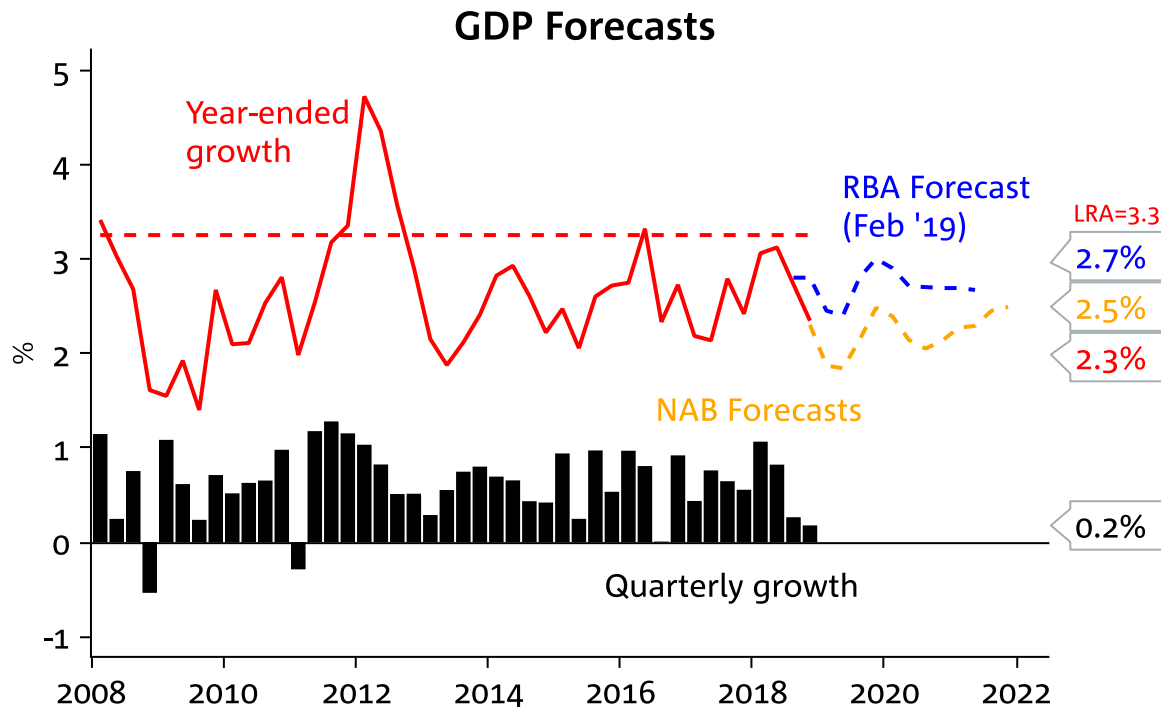


Source: National Australia Bank, Macrobond

INTEREST RATE OUTLOOK – significant change in the outlook for short term interest rates in the US – and longer-term borrowing costs



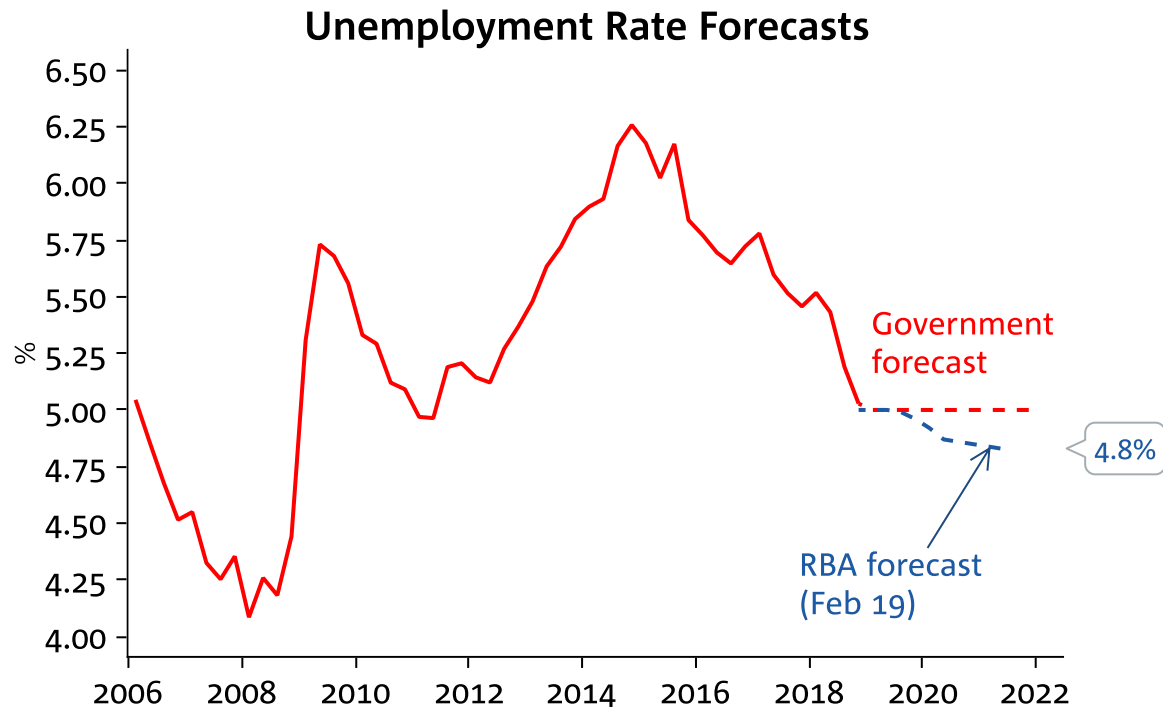
GROWTH - Government forecasts 2.75% GDP for 2019-20; RBA 2.75% for 2019 likely to be revised lower following Q4 GDP



Source: National Australia Bank, ABS

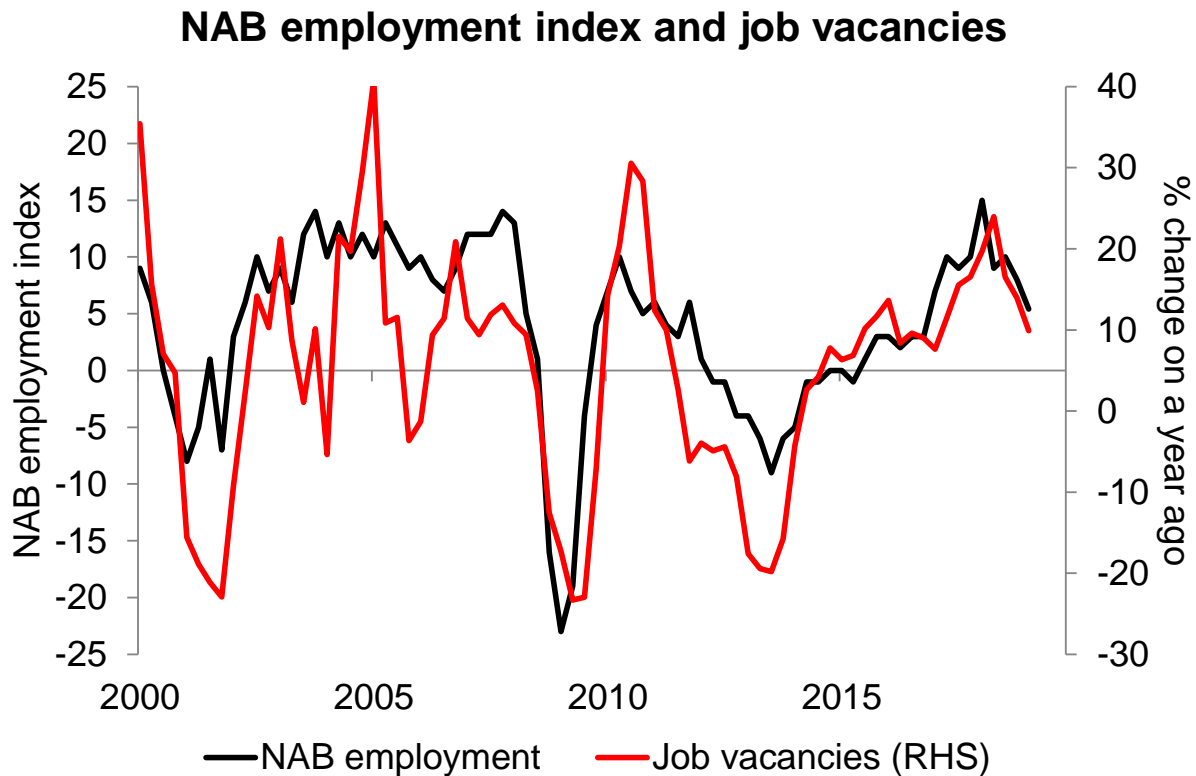
UNEMPLOYMENT

- the unemployment rate has continued to fall, despite slower GDP growth. Government does not forecast further improvement!



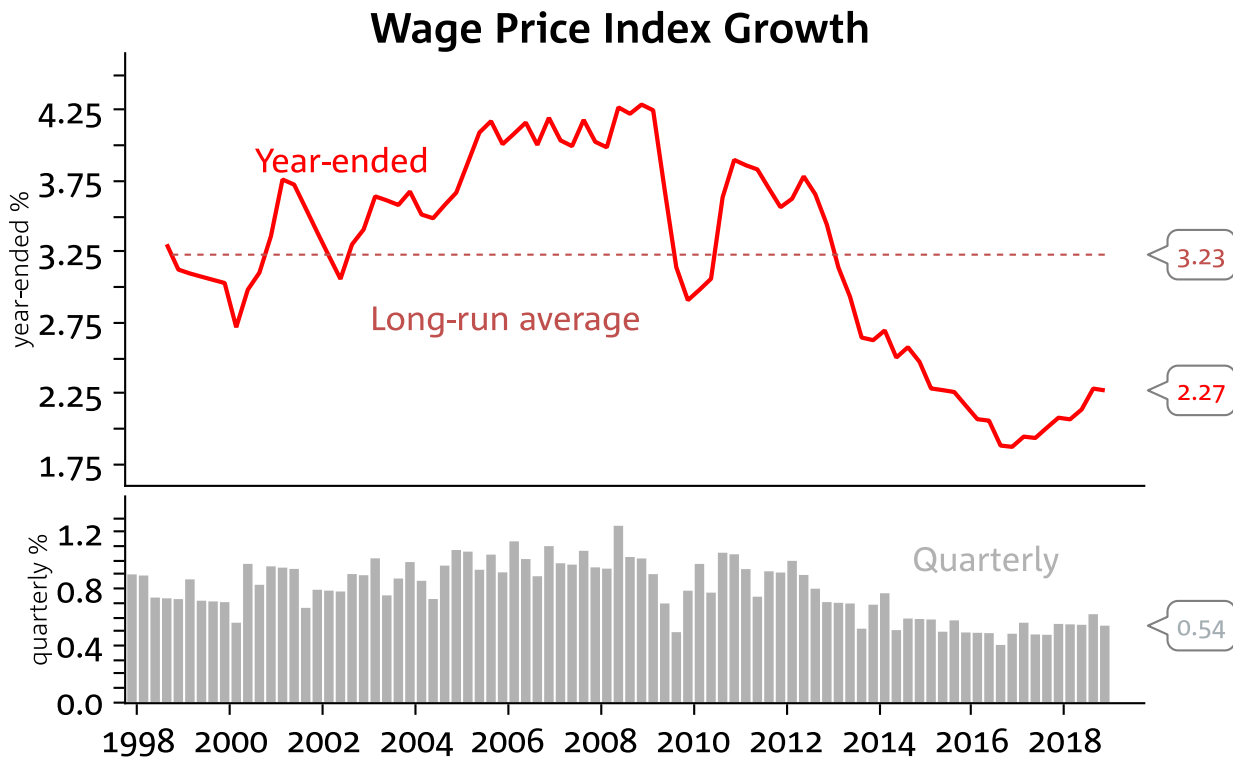
Source: National Australia Bank, ABS, RBA

THE LABOUR MARKET OUTLOOK – job vacancies and the NAB survey provide a better steer than GDP



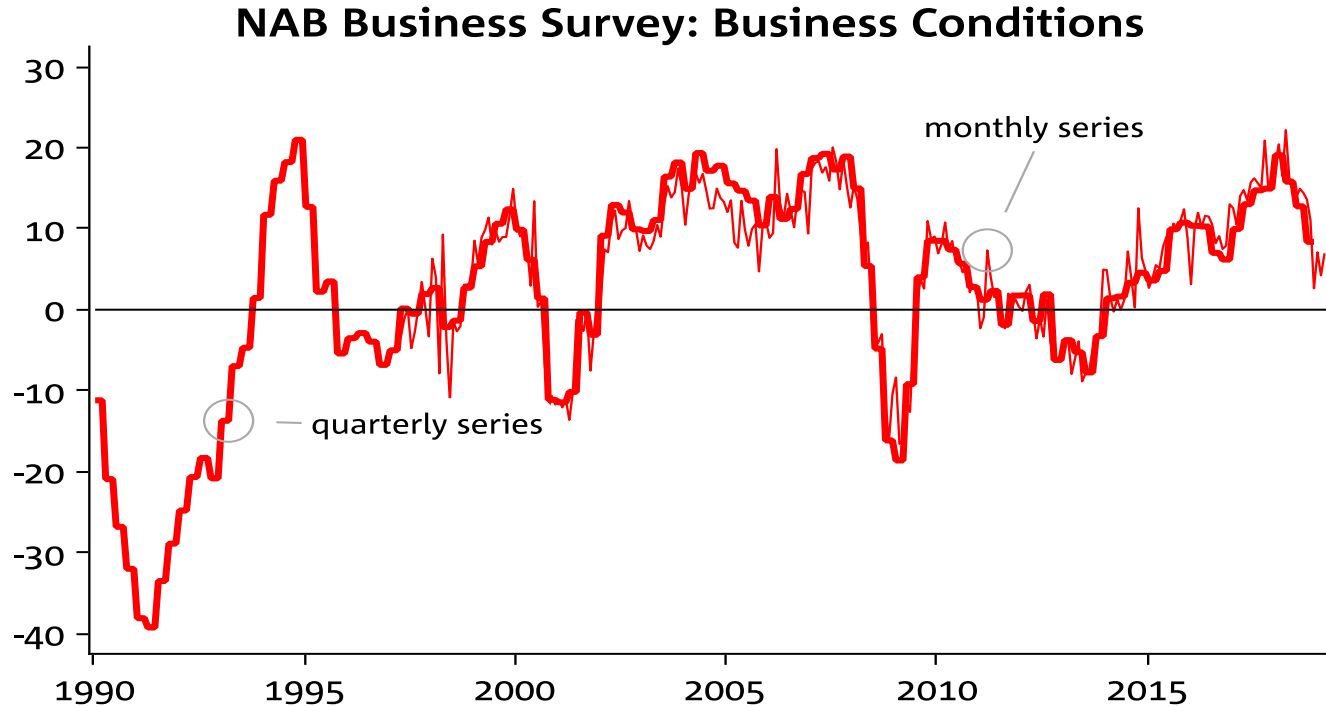
Source: ABS, National Australia Bank

WAGES – still lower unemployment a key pre-requisite for a further pick-up in wages; businesses are continuing to report increased difficulty sourcing suitable labour



Source: National Australia Bank, ABS

AUSTRALIAN BUSINESS CONDITIONS – eased considerably Dec-Feb, but appear to have stabilised at reasonable levels

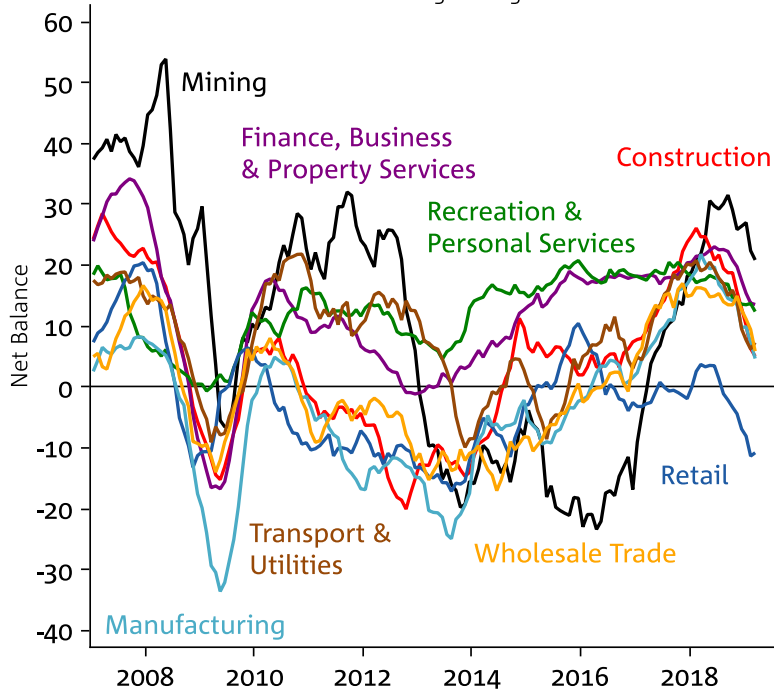


Source: National Australia Bank, Macrobond

BUSINESS CONDITIONS – Mining strongest, retail weakest.

Business Conditions by Industry

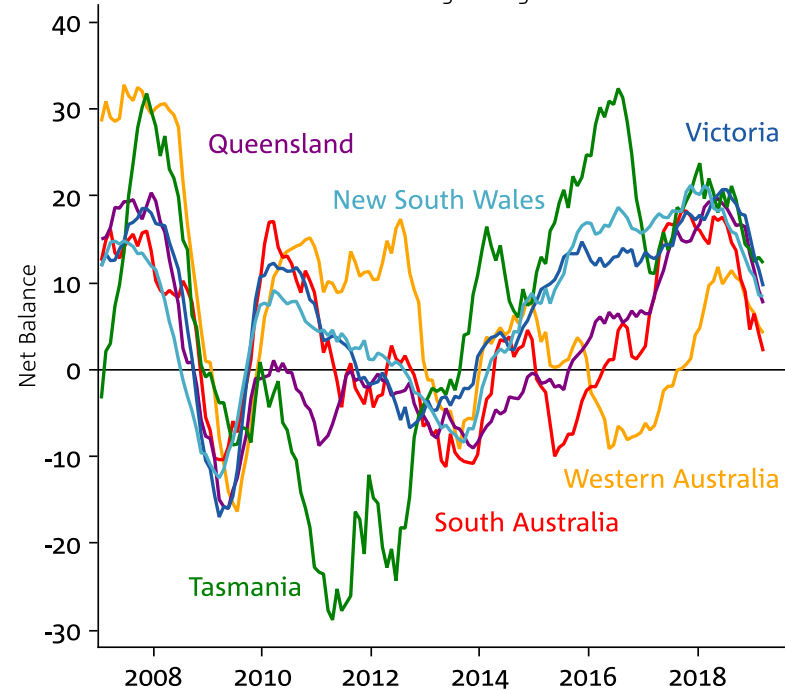
6-month moving average



Source: National Australia Bank

Business Conditions by State

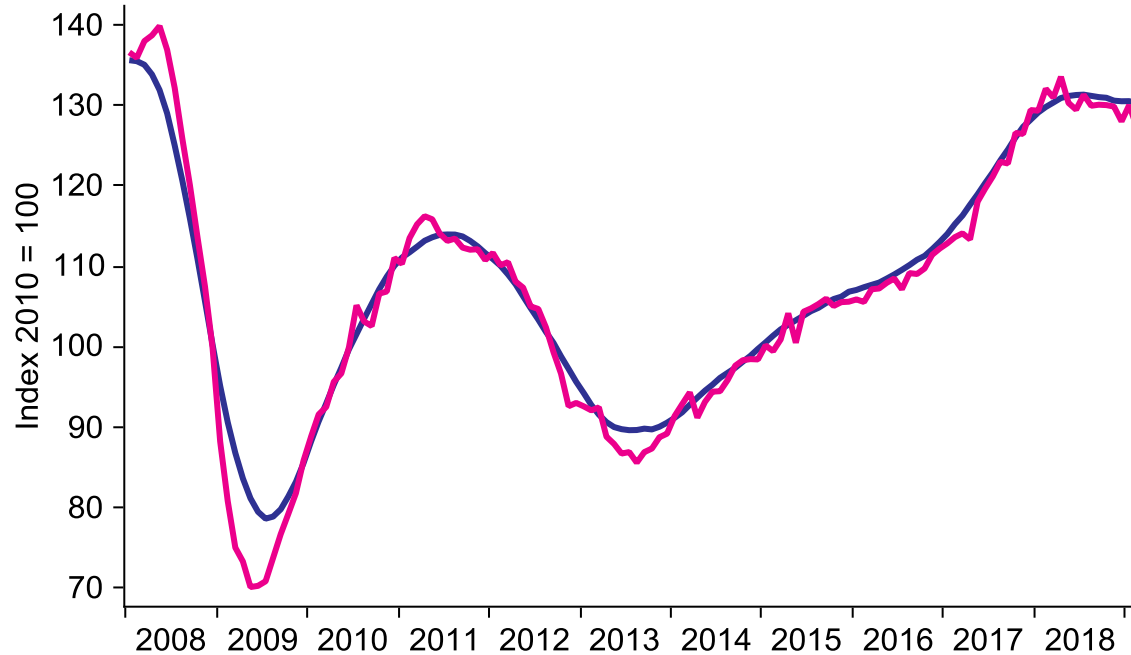
6-month moving average



Source: National Australia Bank

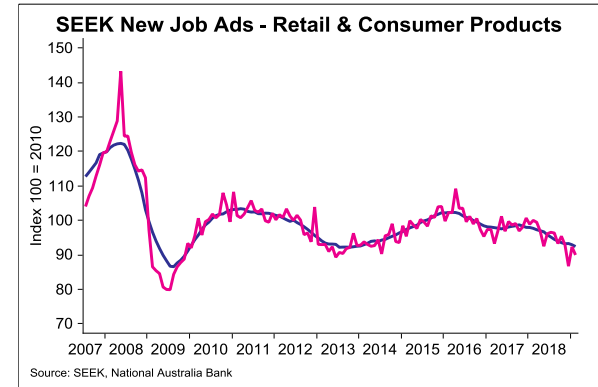
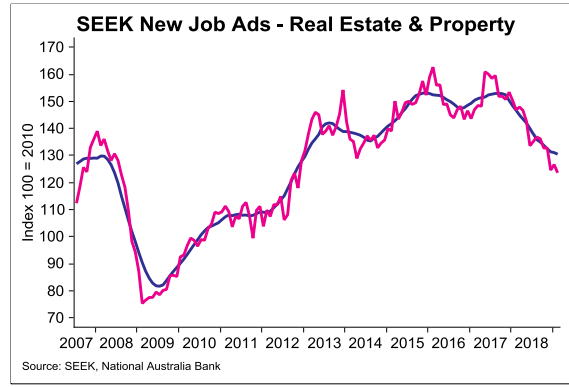
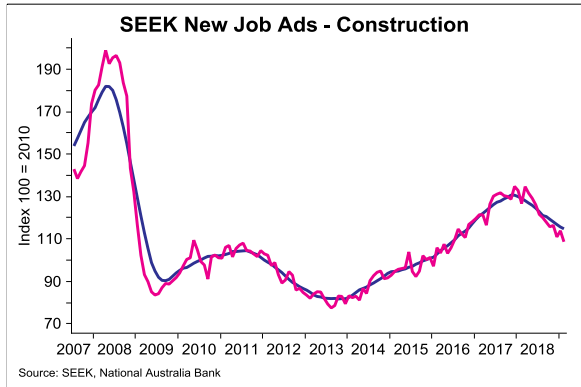
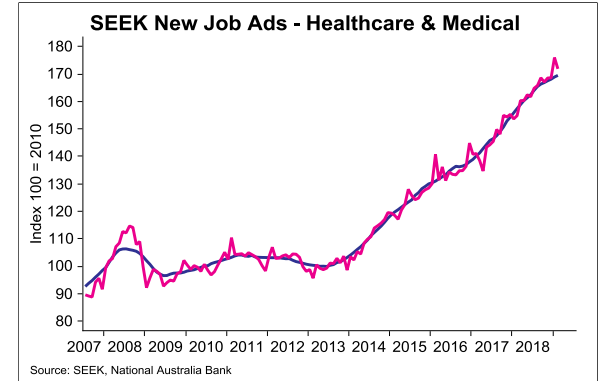
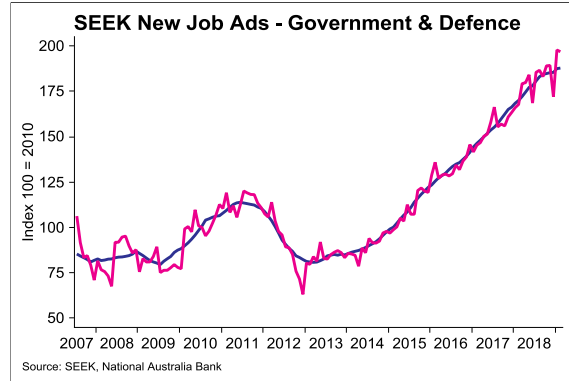
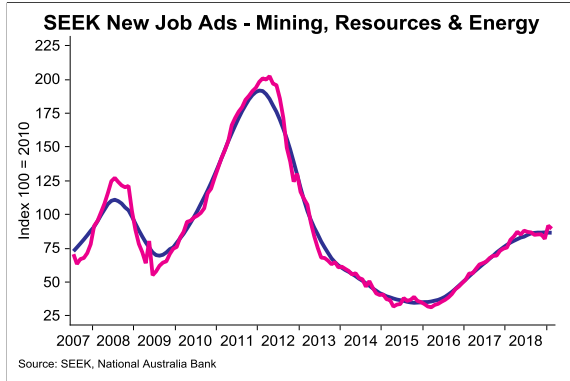
SEEK JOB ADS – *have eased a little in recent months*

SEEK New Job Ads - Australia

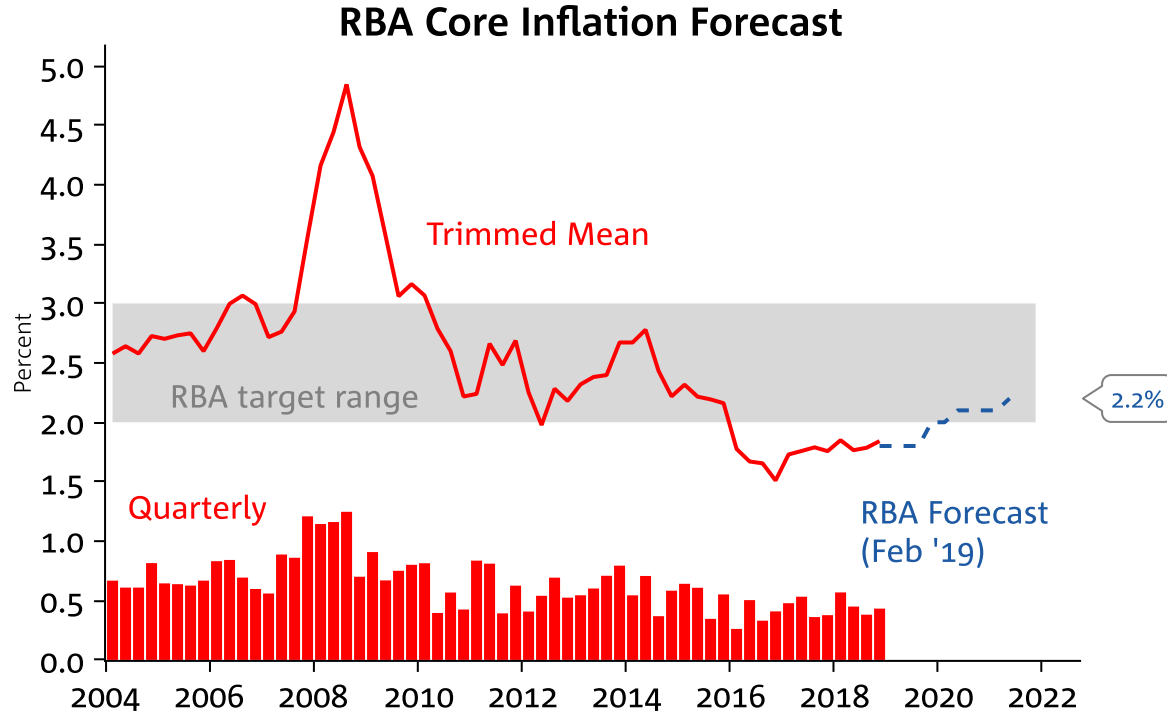


Source: SEEK, National Australia Bank

SEEK JOB ADS – consistent with the sector rotation hypothesis!



INFLATION – RBA (and Government) continue to assume slow track higher (Q1 CPI again likely to be very low)



Source: National Australia Bank, Macrobond

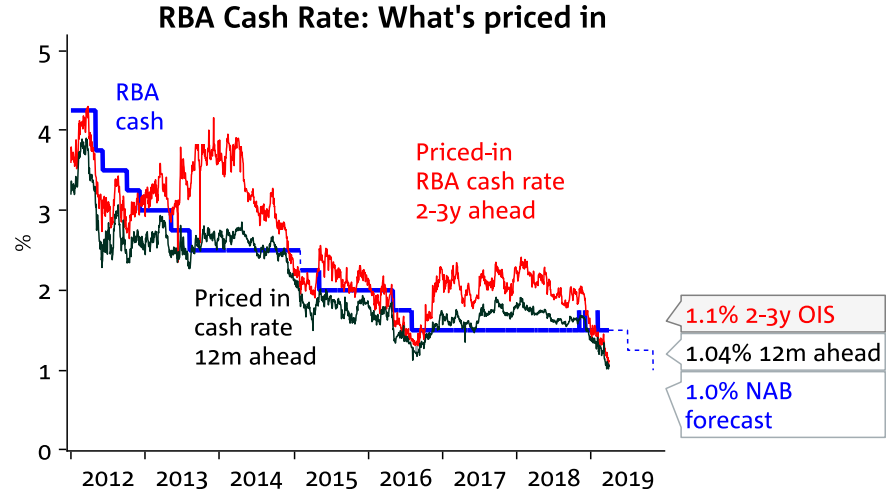
RBA – tension between slower GDP and strong labour market indicators

Recent comments:

- The labour market remains strong
- The GDP data paint a softer picture of the economy than do the labour market data
- The Board will continue to monitor developments and set monetary policy to support sustainable growth in the economy and achieve the inflation target over time

NAB expects:

- Two interest rate cuts before the end of 2019 to support the economy/prevent a rise in unemployment
- Tonight's Budget was not large enough to unwind easing expectations

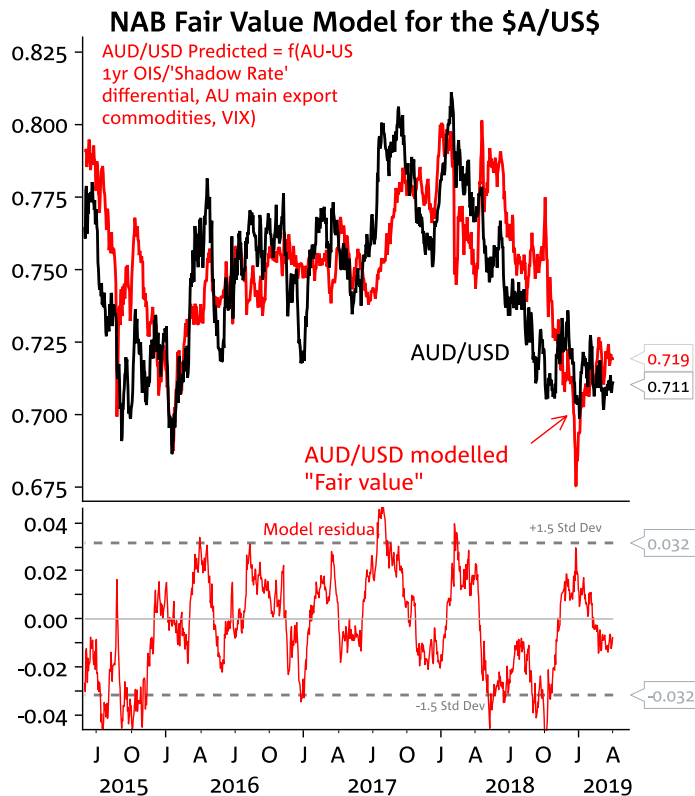


Source: National Australia Bank, Macrobond
OIS is Overnight Indexed Swaps, where the interest payment is compounded from the (overnight/daily) central bank rate

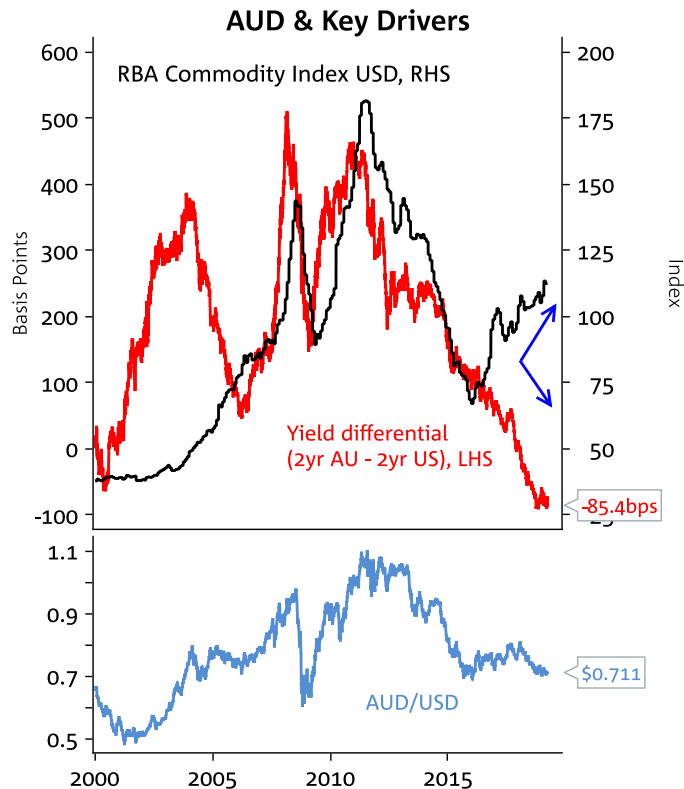
THE AUD REACTED TO THE RBA YESTERDAY BUT NOT THE BUDGET



AUSTRALIAN DOLLAR – NAB fair value model around US\$0.72. Higher commodity prices have broadly offset negative interest rate differentials. \$A expected to trade US\$0.68-0.73 this year.



Source: National Australia Bank, Macrobond



Source: National Australia Bank, Bloomberg

IMPORTANT NOTICES

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