

1.1 BUDGET OUTLOOK

The Context of the 2009-10 Budget Formulation

The 2009-10 Budget has been formulated in an environment of unusual uncertainty for the ACT.

The global financial crisis originating with the failure of US sub-prime mortgages has had profound impacts on the global credit and financial markets. Those in turn have resulted in the most synchronised and sharpest slowdown in the world economy since the great depression of 1930s.

Throughout the formulation of the Budget, the estimates of growth in the world economy have been successively revised downwards. The global economy is now forecast by the IMF to contract by 1.3 per cent in 2009. The Australian national economy is now almost certain to be in recession.

There have been concerted and unprecedented actions from governments around the world to improve liquidity in the credit markets, and to stimulate their respective economies.

Nevertheless, the depth of the recession is difficult to determine, and the timing of the recovery is similarly difficult to predict. While Australia is better placed to withstand the effects of a global recession, an uncertain global economic outlook inevitably leads to an uncertain national economic outlook.

In these global and national economic circumstances, it is to be expected that there will be some impacts on the Territory's economy. Uncertainty in itself has the potential to reduce consumer and business confidence, and investment. Consumer spending and business investment are also likely to be affected by the direct effects of the global financial crisis, such as the availability and cost of credit for business, and loss of asset values.

The ACT economy traditionally performs better than the other jurisdictions during times of national recession, primarily due to its relatively more stable labour market during such times. During the unfolding of the current crisis, the Territory's economy has remained close to full employment.

While there are some signs of softening in the labour market, it has been performing strongly. Unemployment has remained below 3 per cent. Overall, economic growth had been moderating as expected since the extraordinarily strong growth of more than 10 per cent in 2006-07. In 2008-09, State Final Demand (SFD) is forecast to grow by $\frac{3}{4}$ per cent, reflecting a sharper than expected softening in the housing market in the earlier part of the financial year, and relatively flat consumer spending in an environment of increasing interest rates.

Besides the relative stability in the labour market, the Commonwealth Government's stimulus initiatives, along with the ACT Government's local initiatives, are almost certain to have improved consumer spending, and importantly, consumer and business confidence.

Consequences for the Territory's Budget

The impact of the global financial crisis on the Territory's budget has been much more severe than its impacts on the local economy.

The operating budget capacity has significantly reduced due to loss of revenue in 2008-09, and growth over the coming year. The value of financial assets has reduced significantly, in turn reducing income and potentially increasing future costs.

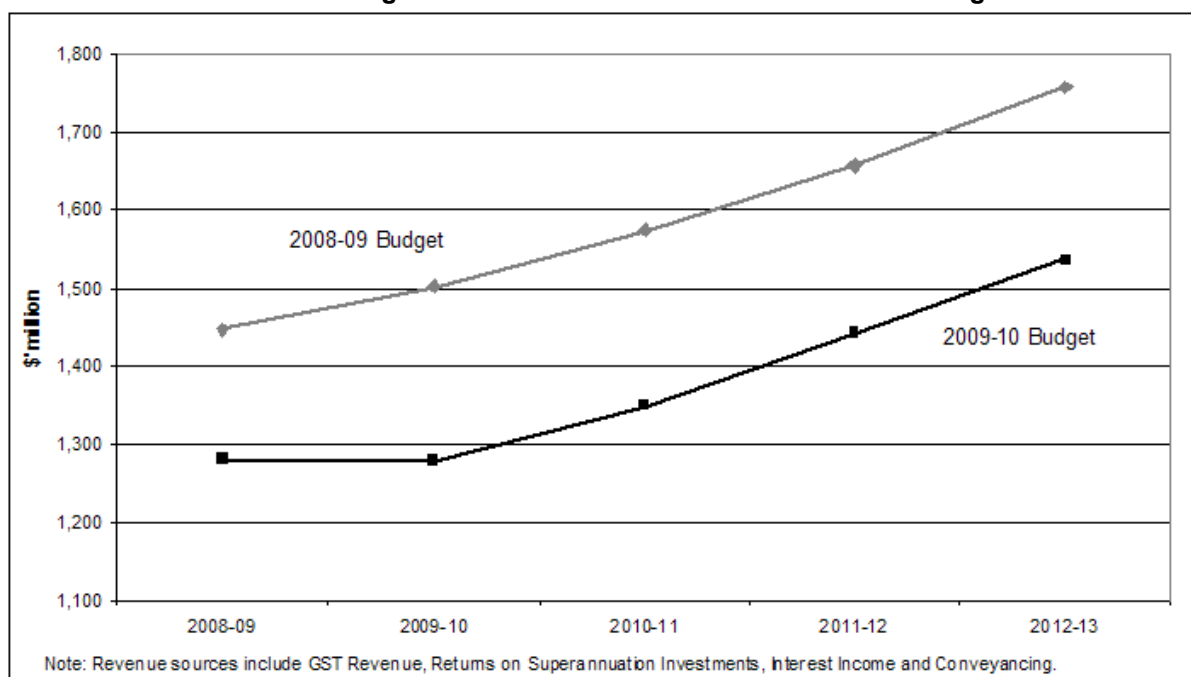
The operating budget has lost revenue growth of around two years over a short period of 6 to 8 months due to the contraction of the national GST pool, loss of income on financial assets, interest earnings on general cash and investments, and subdued activity in the property market.

These sources represent around 44 per cent of the revenue base. The loss of revenue from these sources in 2009-10 is \$224 million, and of similar amounts in the forward years.

The loss of superannuation investment assets is around \$350 million against a forecast growth of \$200 million. The liability is now only 47 per cent funded compared to 65 per cent coverage at June 2008.

The chart below highlights the drop in revenue bases for GST payments from the Commonwealth, return on investments, interest income and conveyancing since the 2008-09 Budget.

Chart 1: Changes in select revenue bases since 2008-09 Budget



The Government had budgeted in the previous years for modest surpluses, in the order of 1.7 per cent of the budget on average. The revenue drop in the above sources represents around 6 per cent of the operating budget.

With expenditures continuing to grow while revenues remain flat over two years, a fiscal gap emerges that is unlikely to be bridged by cyclical recovery alone. A budget adjustment is necessary.

An immediate expenditure adjustment of this magnitude is not possible without severely impacting on service delivery to the community.

The Federal Government's stimulus initiatives, besides having a positive impact on the economy by supporting jobs, benefit the Territory's budget. In particular, investments under the *Nation Building and Jobs Plan* partly replace lost revenues, albeit for the purpose of creating assets in schools and public housing.

Notwithstanding their benefits through partial revenue replacement and asset investment, the Federal Government's stimulus initiatives are not expected to form part of the Territory's base budget over the longer term. The underlying revenue and expenditure aggregates excluding the effects of *Nation Building and Jobs Plan* initiatives, therefore, have been the main reference in developing a plan to return the budget to surplus.

Government's approach to returning the budget to surplus adopts a longer term perspective due to the prevailing circumstances. Those circumstances largely relate to the need to preserve services and provide stability in public expenditure in the current climate. A longer term approach also provides flexibility to adjust to the changing circumstances, allows community consultation on key measures, and avoids any potential overcorrection.

The 2009-10 Budget is underpinned by a Budget Plan that targets achieving a balanced budget by 2015-16. The objectives of the Budget Plan are to ensure that in restoring the budget to surplus, priority services are maintained; and adequate growth in expenditures is allowed to meet the needs of a growing population, and in particular, in the priority service areas such as health and education.

The three main elements contributing to the restoration of the budget under the Plan are savings, expenditure constraint and cyclical recovery. The longer term focus provides flexibility in adjusting the savings task in the context of external factors and the prevailing circumstances.

Under the Budget Plan, the requisite savings are to commence in 2010-11, and completed over the forward estimates period by 2012-13. The 2009-10 Budget incorporates decisions relating to wage restraint and an efficiency dividend that meet a significant part of the savings target for 2010-11 under the Plan.

Further savings will be required in future Budgets over the forward estimates period. The Government will be engaging in community consultation in the lead up to the 2010-11 Budget in order to develop measures which will deliver the remaining (unallocated) savings under the Budget Plan.

Budget and Economic Outlook

The budget forecasts deficits across all the forward years. The underlying Net Operating Balance improves by around \$95 million over the estimates period.

The Budget includes new recurrent policy initiatives totalling \$194.3 million over the estimates period. Those have been almost fully offset by savings of \$152.1 million, and targeted revenue measures totalling \$30.4 million.

The reform of intergovernmental financial relations under the auspices of the Council of Australian Governments (COAG), in particular, the outcomes in relation to Specific Purpose Payments (SPPs), and National Partnerships (NPs) support additional expenditure in the relevant service areas to meet service needs and undertake reforms as agreed by the COAG.

The Budget continues to support the \$1 billion *Building the Future* program, and enhances it with a further \$274 million over four years. The new capital investments will be financed by borrowings.

The Budget Net Operating Balance is presented in Table 1.1.1 below.

Table 1.1.1
General Government Sector — Net Operating Balance

	2009-10 \$'m	2010-11 \$'m	2011-12 \$'m	2012-13 \$'m
Net Operating Balance*	-82.2	-112.4	-164.9	-152.2
Net Impact of Stimulus Initiatives	165.1	96.4	5.0	0
Underlying Net Operating Balance*	-247.3	-208.9	-169.9	-152.2

*The budget net operating balance incorporates the impact of long term superannuation investment earnings to place it on a consistent basis with the GFS estimates presented by state governments. Further details are provided later in this chapter.

Growth in the economy is forecast to recover following the moderation in growth in 2007-08 and 2008-09.

While the unemployment rate is expected to rise from the current 2.8 per cent as a lagged response to the moderating economy in 2008-09, it is still expected to be considerably lower than the national rate. State Final Demand is forecast to grow by 2 per cent.

The ACT unemployment rate is estimated to rise to around 3 per cent at the end of June 2009 and further to 3½ per cent at the end of June 2010. Although the unemployment rate is expected to rise as a lagged response to the moderating economy in 2008-09, it is still expected to remain relatively low compared with unemployment rates across Australia.

The key economic aggregates for the ACT are summarised in Table 1.1.2.

Table 1.1.2
Economic Forecasts, Year-average percentage change

	Actual	Forecasts(a)		Projections (a) (b)		
	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
ACT						
Gross State Product	2.5	1	½	3	3	3
Employment	1	¾	½	1¾	1¾	1¾
State Final Demand	2.2	¾	2	5	5	5

Consumer Price Index	3.6	3½	1¾	2½	2½	2½
Wage Price Index	4.1	3¾	3½	4	4	4
Population(c)	1.3	1¼	1	1	1	1
Australia						
Gross Domestic Product(d)	3.7	1	¾	3	3	3

Notes:

- a) Forecasts and projections are rounded to a ¼ of a percentage point to reflect the relative level of accuracy used in forecasting economic parameters. This is standard forecasting practice used by governments throughout Australia.
- b) Projections are based on long-run averages and are provided for planning purposes only. They do not reflect an expectation (forecast) of actual outcomes. Projections have been updated to reflect changes in the long run trends.
- c) For population forecasts, the December estimate is used to represent the average population for the financial year. As such, the forecast growth is based on the growth from one December to the next, rather than 'year average' as with all other forecasts.
- d) Commonwealth Government forecasts are provided in the 2008-09 Updated Economic and Fiscal Outlook published in February 2009.

Overview of the 2009-10 Budget

The 2009-10 Budget includes:

- A forecast General Government Sector Net Operating Deficit of \$82.2 million in 2009-10.
- The underlying deficit (net of Commonwealth Government stimulus revenue) is *minus* \$247.3million in 2009-10, while the deficit is *minus* \$152.2 million in 2012-13 under either measure.
- The 2009-10 Budget is underpinned by a Budget Plan that targets achieving a balanced budget by 2015-16.
- A Strong General Government Sector Balance Sheet, with
 - Net Financial Worth of \$3.2 billion; and
 - Net Financial Liabilities of \$2.1 billion.
- Maintenance of Operating Cash surpluses across all years.
- Expenditure initiatives totalling \$194.3 million over four years, across a number of priority areas of need.
- Significant capital investment capacity with infrastructure programs and projects of \$928.4 million over 4 years. Of this amount \$243.6 million is an allocation of the *Building the Future* provisions.
- Specifically, the new capital works program and projects includes:
 - new construction works of \$742 million across the Budget and forward estimates;
 - feasibility and forward design projects of \$8.9 million;
 - capital upgrades expenditure of \$44.3 million in 2009-10;
 - capital grants totalling \$8.5 million across the budget and forward estimates;
 - new information and communication technology (ICT) initiatives with a total of \$107.3 million; and
 - new plant and equipment initiatives with a total value of \$17.4 million over four years.
- An estimated \$333 million of capital works in 2008-09 - a record achievement.
- Estimated borrowings of \$400 million by the end of 2010-11.

