

PRE-ELECTION ECONOMIC AND FISCAL OUTLOOK

OVERVIEW

The Australian economy is expected to grow by 4¼ per cent in 2007-08 despite the ongoing effects of drought and heightened downside risks to the world economic outlook.

The underlying cash and fiscal balances are estimated to be in surplus in 2007-08 and the forward years. Table 1 provides revised estimates and projections of the underlying cash and fiscal balances for the period from 2007-08 to 2010-11.

Table 1: Summary of budget aggregates

	Estimates		Projections	
	2007-08	2008-09	2009-10	2010-11
Underlying cash balance (\$b)(a)	14.4	14.3	17.7	15.0
Per cent of GDP	1.3	1.2	1.4	1.2
Fiscal balance (\$b)	14.4	13.6	18.4	17.1
Per cent of GDP	1.3	1.1	1.5	1.3

(a) Excludes expected Future Fund earnings.

ECONOMIC OUTLOOK

The Australian economy is forecast to grow by 4¼ per cent in 2007-08 and 3½ per cent in 2008-09. Growth is expected to be broadly based, reflecting continued strong business investment and household consumption. A partial recovery from drought is forecast to contribute to GDP growth, although dry weather conditions and low water storage levels pose a downside risk to the farm outlook. Farm production is not expected to recover to pre-drought levels over the forecast horizon.

In line with the forecasts for GDP growth, employment is expected to grow by 2¼ per cent in 2007-08 before easing to 1¾ per cent in 2008-09. Wage and inflation pressures in the near-term are expected to ease over the forecast horizon.

Strong world growth, particularly in emerging market economies, is expected to support the domestic economy. However, the potential for further financial market volatility associated with the US sub-prime mortgage market poses a downside risk to the outlook.

Table 2 presents the major economic parameters used in preparing the *Pre-Election Economic and Fiscal Outlook 2007* (PEFO). The parameters for 2007-08 and 2008-09 are forecasts, while those for 2009-10 and 2010-11 are projections. The forecast assumptions and projection methodology are consistent with those in the *Mid-Year Economic and Fiscal Outlook 2007-08* (2007-08 MYEFO). As noted in the 2007-08 MYEFO,

if the recent financial market turbulence continues to be resolved in a relatively benign fashion, stronger outcomes are possible for the domestic economy, especially given the magnitude of investment projects in the pipeline. Stronger growth in an economy that is close to full employment could add to wage and price pressures, although if the recent appreciation of the Australian dollar is sustained, this would have a dampening effect on economic activity and prices.

A more detailed discussion of the economic outlook is contained in the 2007-08 MYEFO.

Table 2: Major economic parameters^(a)

	Forecasts		Projections	
	2007-08	2008-09	2009-10	2010-11
Real GDP	4 1/4	3 1/2	3	3
Employment	2 1/4	1 3/4	1 1/4	1 1/4
Wage Price Index	4 1/4	4 1/4	4	4
CPI	2 3/4	2 3/4	2 1/2	2 1/2

(a) Year-average percentage change.

FISCAL OUTLOOK

An underlying cash surplus of \$14.4 billion, or 1.3 per cent of GDP, is estimated for 2007-08. A fiscal surplus of \$14.4 billion, or 1.3 per cent of GDP, is estimated for 2007-08. The fiscal outlook is for continuing underlying cash and fiscal surpluses in the forward years. This is consistent with the outlook published in the 2007-08 MYEFO, after reflecting the impact of decisions taken prior to the dissolution of Parliament.

Table 3 provides a summary of the major budget aggregates.

Table 3: Australian Government general government sector budget aggregates^(a)

	Estimates		Projections	
	2007-08	2008-09	2009-10	2010-11
Revenue (\$b)	251.9	264.0	278.7	287.5
Per cent of GDP	22.5	22.1	22.4	22.1
Expenses (\$b)	235.8	248.7	259.4	269.5
Per cent of GDP	21.0	20.8	20.8	20.8
Net operating balance (\$b)	16.0	15.3	19.3	18.0
Net capital investment (\$b)	1.6	1.8	1.0	0.9
Fiscal balance (\$b)	14.4	13.6	18.4	17.1
Per cent of GDP	1.3	1.1	1.5	1.3
Underlying cash balance (\$b)(b)	14.4	14.3	17.7	15.0
Per cent of GDP	1.3	1.2	1.4	1.2
<i>Memorandum item:</i>				
Headline cash balance (\$b)	22.3	18.3	19.1	16.3

(a) All estimates are based on Government Finance Statistics (GFS) standards, but with goods and services tax (GST) revenue collected on behalf of the States and Territories netted off revenue and expenses.

(b) Excludes expected Future Fund earnings.

Table 4 provides a reconciliation of the fiscal balance estimates between the 2007-08 Budget, the 2007-08 MYEFO and the 2007 PEFO.

Table 4: Reconciliation of 2007-08 Budget, 2007-08 MYEFO and 2007 PEFO fiscal balance estimates^(a)

	Estimates		Projections	
	2007-08	2008-09	2009-10	2010-11
	\$m	\$m	\$m	\$m
2007-08 Budget fiscal balance	9,999	11,860	14,101	13,704
Per cent of GDP	0.9	1.0	1.2	1.1
Changes between 2007-08 Budget and MYEFO				
Effect of policy decisions(b)	-3,909	-10,766	-13,748	-17,836
Effect of parameter and other variations	8,792	12,548	18,062	21,256
Total variations	4,883	1,781	4,314	3,421
2007-08 MYEFO fiscal balance	14,882	13,642	18,415	17,125
Per cent of GDP	1.3	1.1	1.5	1.3
Changes between 2007-08 MYEFO and PEFO				
Effect of policy decisions(b)				
Revenue	-2	24	-1	-1
Expenses	380	84	1	35
Net capital investment	5	3	-1	-2
Total policy decisions impact on fiscal balance	-387	-64	0	-35
Effect of parameter and other variations				
Revenue	-11	-31	-35	-38
Expenses	49	-7	-6	-6
Net capital investment	0	0	0	0
Total parameter and other variations impact on fiscal balance	-61	-24	-29	-33
2007 PEFO fiscal balance	14,435	13,554	18,386	17,057
Per cent of GDP	1.3	1.1	1.5	1.3

(a) A positive number for revenue indicates an increase in the fiscal balance, while a positive number for expenses and net capital investment indicates a decrease in the fiscal balance.

(b) Excludes the public debt net interest effect of policy measures.

Table 5 provides a list of the policy decisions taken and parameter and other variations from 10 October 2007 (reflecting the inclusion of policy decisions taken up to and including 9 October 2007 in the 2007-08 MYEFO) to the commencement of the caretaker period on 17 October 2007.

Table 5: Variations since the 2007-08 MYEFO^(a)

	2007-08 \$m	2008-09 \$m	2009-10 \$m	2010-11 \$m
POLICY DECISIONS				
Revenue measures				
Australian Defence Force – reclassification of service by Australian Training Support Team in East Timor	-1.6	..	-	-
Capital gains tax – changes to small business concessions	*	*	*	*
Capital gains tax – demutualisation of health insurers	-	26.3	2.0	1.0
Capital gains tax – ending of interests in widely held entities and the market value substitution rule	*	*	*	*
Commencement date for changes to the consolidation tax cost settling rules	*	*	*	*
Equine influenza – twelve week extension of assistance	-	-	-	-
Personal income tax – tax exemption for the Queensland Government's \$1,000 Early Completion Bonus for apprentices	-0.6	-0.7	-0.8	-0.8
Philanthropy – changes to prescribed private funds	-	-1.1	-0.6	-1.0
Philanthropy – updating the list of deductible gift recipients	-	-1.0	-1.1	-0.6
Total revenue measures	-2.2	23.6	-0.5	-1.4
Expense measures				
Aged Care – increase funding for the National Seniors Association	0.2	0.2	0.2	0.2
Australian Defence Force – inclusion of the Australian Training Support Team in the United Nations Transitional Administration in East Timor	0.6	0.6	0.8	0.9
Australian Made Campaign – additional funding	0.9	0.9	0.9	-
Australian Paralympic Committee – additional contribution	3.5	6.5	5.5	5.5
Australian Red Cross Blood Service – support The Year of the Blood Donor initiative	2.0	-	-	-
Bass Strait Passenger Vehicle Equalisation Scheme – increase the standard passenger vehicle rebate from \$150 to \$168 each way	2.6	2.9	2.9	2.9
Beaconsfield Community Fund – additional funding for Grubb Shaft Gold and Heritage Museum	0.3	-	-	-
Bimbimie Wildlife Park – support for infrastructure costs(b)	-	-	-	-
Bradman Centenary Project – contribution to the construction of two new wings at the Bradman Museum	3.3	3.3	-	-
Bravery medals from the Battle of Long Tan – establishment of review panel	0.2	-	-	-
Brendan's Fund – ex-gratia payment	0.4	-	-	-
Centre for Social Impact – matching contribution to the initial endowment to establish the Centre	12.5	-	-	-
Chamber Music Australia – contribution	0.1	-	-	-
Clever Networks – additional funding for connecting independent Victorian schools(c)	-	-	-	-
Clinical School at Greenslopes Private Hospital	11.7	1.3	-	-
Commonwealth Trade Learning Scholarship – extension of scholarship for early completion of apprenticeship	0.3	0.4	0.4	0.4
Community Water Grants – bring-forward of expenditure	105.0	-10.0	-49.9	-45.2
Cricket Australia Centre of Excellence – contribution	1.0	5.5	11.0	-
Drought assistance – Exceptional Circumstances assistance for primary producers – additional declarations	1.7	2.7	..	-
Drought assistance – Exceptional Circumstances assistance for small business – additional declarations	0.2	0.3	-	-
Employer and apprentice incentives for apprentices in skills shortage – remove the prior-qualification rule	0.8	7.4	8.6	9.8
Employer incentives for intermediate qualifications	0.1	1.0	1.1	0.7
Equine influenza – twelve week extension of assistance	116.8	-	-	-

Table 5: Variations since the 2007-08 MYEFO^(a) (continued)

	2007-08	2008-09	2009-10	2010-11
	\$m	\$m	\$m	\$m
Expense measures (continued)				
General Employee Entitlements and Redundancy Scheme – continue funding liquidators to pursue litigation	-	8.0	-	-
Great Barrier Reef Marine Park Structural Adjustment Package – additional funding	50.8	-	-	-
Immigration Health Screening Process – strengthening	6.7	7.9	6.1	6.2
Innovative rainfall enhancement technology – contribution to operational trials	10.0	-	-	-
Kokoda Track – assistance to Papua New Guinea for World Heritage listing of the Owen Stanley Ranges(d)	0.5	5.4	3.5	3.5
Living Away From Home Allowance – extension to Australian school-based apprentices	0.1	-	-	-
Local government amalgamation – plebiscites in the Northern Territory(e)	*	*	*	*
Medicare Benefits Schedule – make knee and brain Magnetic Resonance Imaging services referred by General Practitioners Medicare-eligible	1.5	4.1	3.8	3.7
Netball Australia – additional funding	1.6	0.4	0.4	-
Operations Catalyst and Slipper – enhanced electronic counter measures(f)	-	-	-	-
Orang-utan conservation in Indonesia – funding(g)	-	-	-	-
Pambula Surf Life Saving Club – contribution	0.1	-	-	-
Patrol vessel in Australian Northern Waters – extension	10.4	24.2	-	-
Pharmaceutical Benefits Scheme – extension to the listing of Remicade®	3.6	6.8	6.6	8.6
Pharmaceutical Benefits Scheme – extension to the listing of Topamax®	6.1	10.8	11.0	11.2
Pharmaceutical Benefits Scheme – listing of Renegal®	6.9	15.2	20.1	22.9
Punt Road Oval – contribution	0.5	1.5	-	-
Ray Owen Sports Centre – contribution	0.2	-	-	-
Regional maritime security capacity-building(d)	0.9	2.4	2.4	2.1
Reversal of a measure reported as a 'decision taken but not yet announced' in the 2007-08 MYEFO	-10.0	-26.0	-36.0	-
Seniors Concession Allowance – increase(h)	-	-	-	-
Sydney 2009 World Masters Games – contribution	8.5	-	-	-
Sydney Dance Company – contribution	1.5	-	-	-
Television Technical Operators College and Westrac National Skills Training Centre of Excellence – grants	16.2	-	-	-
Utilities Allowance – increase and extend eligibility to include all recipients of Disability Support Pension, Service Pension and Carer Payment(i)	-	-	-	-
Depreciation expense(j)	0.1	0.8	1.5	1.5
Total expense measures(k)	379.9	84.3	0.7	34.9
Capital measures				
Australian Defence Force – inclusion of the Australian Training Support Team in the United Nations Transitional Administration in East Timor	0.2	-	-	-
Immigration Health Screening Process – strengthening	3.6	3.6	-	-
Patrol vessel in Australian Northern Waters – extension	0.9	0.1	-	-
Depreciation expense(j)	-0.1	-0.8	-1.5	-1.5
Total capital measures(k)	4.6	2.9	-1.5	-1.5
Total policy decisions impact on fiscal balance	-386.7	-63.7	0.2	-34.7

Table 5: Variations since the 2007-08 MYEFO^(a) (continued)

	2007-08	2008-09	2009-10	2010-11
	\$m	\$m	\$m	\$m
PARAMETER AND OTHER VARIATIONS				
Revenue variations				
Other	-11.3	-31.0	-34.9	-38.4
Total revenue variations	-11.3	-31.0	-34.9	-38.4
Expense variations				
Department of Immigration and Citizenship funding base adjustment – annual funding reconciliation	49.3	-	-	-
Drawdown of the contingency reserve Official Development Assistance provision(d)	-	-7.4	-5.9	-5.6
Total expense variations	49.3	-7.4	-5.9	-5.6
Total parameter and other variations impact on fiscal balance	-60.6	-23.6	-29.0	-32.8
TOTAL VARIATIONS SINCE THE 2007-08 MYEFO IMPACT ON FISCAL BALANCE	-447.3	-87.3	-28.8	-67.5

* The nature of the measure is such that a reliable estimate cannot be provided.

.. Not zero, but rounded to zero.

- Nil.

(a) A positive number for revenue indicates an increase in the fiscal balance, while a positive number for expenses and net capital investment indicates a decrease in the fiscal balance.

(b) The *Bimbimie Wildlife Park — support for infrastructure costs* measure includes funding of \$2.5 million in 2007-08. This funding will be met from within the existing resourcing of the Department of the Environment and Water Resources.

(c) The *Clever Networks — additional funding for connecting independent Victorian schools* measure includes funding of \$2.0 million in 2007-08 and \$3.0 million in 2008-09. This funding will be met from within the existing resourcing of the Department of Communications, Information Technology and the Arts.

(d) The *Drawdown of the contingency reserve Official Development Assistance provision* estimates variation partially offsets the *Kokoda Track — assistance to Papua New Guinea for World Heritage listing of the Owen Stanley Ranges and Regional maritime security capacity-building* measures.

(e) The *Local government amalgamation — plebiscites in the Northern Territory* measure funding is unquantifiable at this stage as it will depend on the number of local government areas included in the plebiscites and the format for the plebiscites.

(f) The *Operations Catalyst and Slipper — enhanced electronic counter measures* measure includes funding of \$46.0 million in 2007-08 and \$27.0 million in 2008-09. This funding will be met from within the existing resourcing of the Department of Defence.

(g) The *Orang-utan conservation in Indonesia — funding* measure includes funding of \$500,000 over four years. This funding will be met from within the existing resourcing of AusAID.

(h) The *Seniors Concession Allowance — increase* measure includes funding of \$36.0 million in 2007-08, \$65.0 million in 2008-09, \$63.0 million in 2009-10 and \$65.0 million in 2010-11. This measure was included as a 'decision taken but not yet announced' in the 2007-08 MYEFO.

(i) The *Utilities Allowance — increase and extend eligibility to include all recipients of Disability Support Pension, Service Pension, and Carer Payment* measure includes funding of \$504.0 million in 2007-08, \$1,041 million in 2008-09, \$1,077 million in 2009-10 and \$1,122 million in 2010-11. This measure was included as a 'decision taken but not yet announced' in the 2007-08 MYEFO.

(j) Aggregate depreciation expenses in relation to capital measures.

(k) Measures may not add due to rounding.

Cash flows

In 2007-08, an underlying cash surplus of \$14.4 billion is expected. New policy decisions and parameter and other variations since the 2007-08 MYEFO have had a similar impact on the underlying cash balance as the fiscal balance.

Table 6: Reconciliation of 2007-08 Budget and 2007 PEFO underlying cash balance estimates

	Estimates		Projections	
	2007-08 \$m	2008-09 \$m	2009-10 \$m	2010-11 \$m
2007-08 Budget underlying cash balance(a)	10,637	12,712	13,812	12,447
Changes from 2007-08 Budget to MYEFO				
Effect of policy decisions(b)	-3,886	-10,840	-13,859	-17,996
Effect of parameter and other variations	8,083	12,525	17,776	20,638
Total variations	4,197	1,685	3,917	2,642
2007-08 MYEFO underlying cash balance(a)	14,834	14,396	17,729	15,089
Changes from 2007-08 MYEFO to PEFO				
Effect of policy decisions(b)	-406	-53	11	-35
Effect of parameter and other variations	-61	-24	-29	-33
Total variations	-467	-77	-18	-68
2007 PEFO underlying cash balance(a)	14,367	14,319	17,711	15,021

(a) Excludes expected Future Fund earnings.

(b) Excludes the public debt net interest effect of policy measures.

Statement of risks and sensitivity of fiscal expenses and revenues to economic developments

The statement of risks and the estimated sensitivity of the fiscal aggregates to changes to the economic parameters for the 2007 PEFO are unchanged from that provided in the 2007-08 MYEFO. They are therefore not included in this report. The 2007-08 MYEFO statement of risks updated those material fiscal risks and contingent liabilities that had changed since the 2007-08 Budget.