30 September 2024

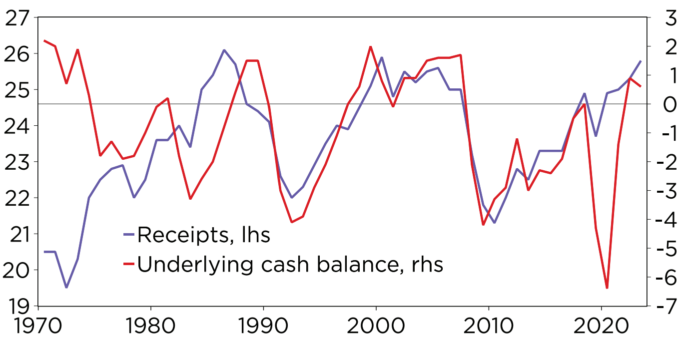
AUSTRALIAN FEDERAL BUDGET BULLETIN

Final budget outcome 2023/24

Key points

- The Federal government notched up its second consecutive surplus of $15.8bn (or 0.6% of GDP) in 2023-24.
- Temporary factors, including high commodity prices, high (but moderating) inflation and the resulting bracket creep combined to keep real tax per person at a record high, and so generate a "budget sweet spot" that helped deliver consecutive surpluses.
- These factors are now clearly fading, at a time when spending pressures have grown and are expected to grow further. Last time receipts to GDP were around current levels, the government recorded surpluses of around 2.0% of GDP, showing the extent of the spending pressures.
- Going forward, off budget and state spending are likely to account for a more important share of the national fiscal impulse.

Underlying cash balance and receipts



Source: Australian Department of the Treasury, Macrobond, Westpac Economics

> "In this environment, the Government's approach of banking as much of these windfalls as possible is spot on."

Second surplus before a sea of red

Pat Bustamante
Senior Economist

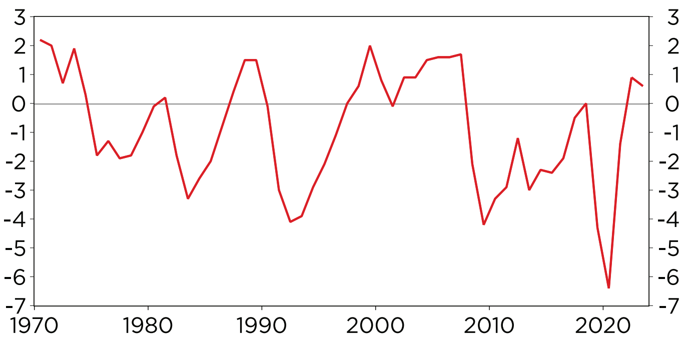
The Federal government notched up its second consecutive surplus in 2023-24. The $15.8bn (0.6% of nominal GDP) underlying cash surplus was slightly down on the surplus of $22.1bn recorded in 2022-23, but $6.4bn better than what was expected back in the May budget.

Payments came in $10.2bn lower than expected, with the majority of this driven by delays in outflows to the states through National Partnership Agreements ($4.2bn); and in other government programs such as the Support Reliable, Secure and Affordable Energy and Indigenous Advancement programs.

Total receipts were $3.7bn lower than expected back in May, mainly driven by lower-than-expected personal income taxes ($3.1bn lower) – another sign the labour market is indeed softening.

Underlying cash balance

% of nominal GDP

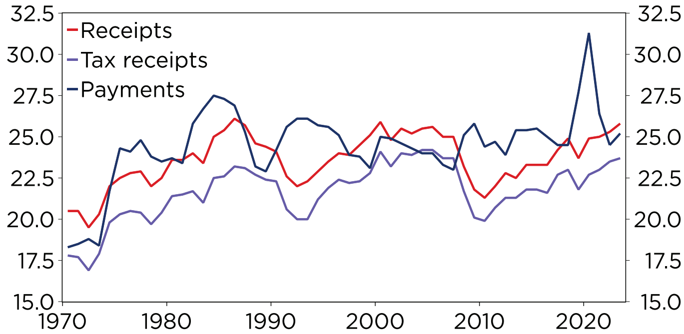


Source: Australian Department of the Treasury, Macrobond, Westpac Economics

Stepping back, the narrative remains broadly unchanged. The Federal budget has been in a temporary budget sweet spot. Today's Final Budget Outcome confirms Government receipts (mainly tax receipts) as a share of nominal GDP was around a record high of 25.8% in 2023-24 (record was 26.1% in 1986). Bracket creep, high commodity prices and high inflation are all supporting the Government's tax take.

Budget aggregates

% of nominal GDP

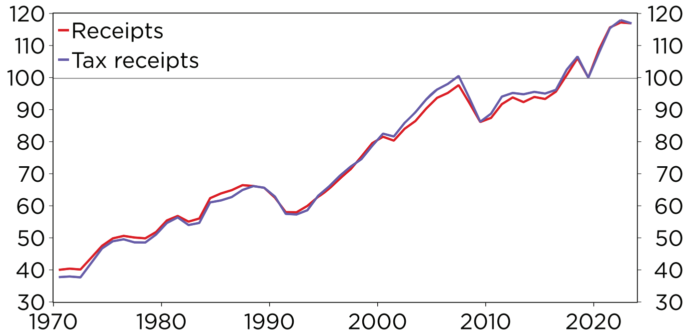


Source: Australian Department of the Treasury, Macrobond, Westpac Economics

The impact of bracket creep is particularly noticeable. Real (that is, adjusted for inflation) government receipts per person are sitting around a record high, and around 17% higher than in 2019 before the onset of the pandemic. This is clearly contributing to the squeeze on household income.

Real receipts per person

Index: 2019 = 100



Source: Australian Department of the Treasury, Macrobond, Westpac Economics

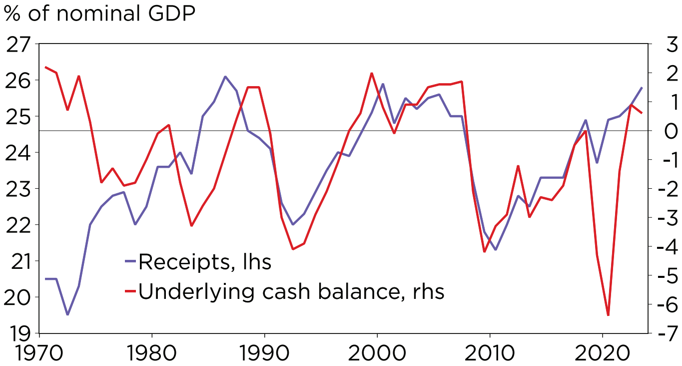
But these temporary factors are now fading. Stage 3 tax cuts are expected to give back around $23bn in bracket creep this financial year (2024-25). Commodity prices continue to be volatile but have eased compared with the levels recorded a year ago. And inflation is moderating which will slow growth in indirect taxes such as GST collections.

At the same time, pressures on the payment side of the budget continue to grow. Geopolitical instability, economic uncertainty and demographic trends (most notably the ageing of the population) have combined to see governments become a larger part of the economy.

In this environment, the Government's approach of banking as much of these windfalls as possible is spot on. But this approach has had to be managed against growing spending pressures.

The extent of these spending pressures can be seen below. Last time receipts to GDP were running at a similar level (25.9% in 1999-200), the underlying cash surplus was sitting at around 2.0% of nominal GDP. Going forward, the Government's May forecasts have the budget tipping back into the red as spending pressures come to the fore and the temporary windfalls fade, projecting deficits across the forward estimates (2027-28) and medium term (2034-35).

Underlying cash balance and receipts



Source: Australian Department of the Treasury, Macrobond, Westpac Economics

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Assessing the policy stance going forward

Multiple levers

Unlike monetary policy where the RBA has one policy lever to manage demand, governments have several levers that can be used to achieve policy priorities. Off budget spending, providing explicit guarantees, entering arrangements with the states and changing regulations are all levers the government can use, which are unlikely to directly impact the underlying cash balance.

Off budget spending usually involves the government "spending" through a third party. For example, the government provided Housing Australia with $282m in 2023-24, which Housing Australia has used to build or acquire affordable housing. This impacted the headline and not the underlying cash balance. Off budget spending was around $1.8bn in 2023-24, lower than the $2.9bn expected back in the May budget.

Back in May, the government forecast a large increase in off budget spending to $18.9bn in 2024-25, suggesting that this mechanism will become more important going forward.

Interactions with the states

The Federal surplus is expected to be partly offset by deficits across the states. This is not a coincidence. The growth in the population through higher migration and international students add to tax revenue but has limited impacts on federal payments, at least initially.

On the other hand, states are responsible for delivering infrastructure, public health services and public schooling where demands have increased due to the growing population. As infrastructure investment and public services continue to catch up to the growth in the population, state spending is likely to become a more important component of the national fiscal impulse.

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