



Friday, 21 March 2025

# 2025–26 AUSTRALIAN FEDERAL BUDGET PREVIEW

Some pre-election sweeteners but no lolly scramble

## Key points

- Next week's Federal Budget is shaping as an 'awkward' one in terms of both timing, fiscal constraints and tensions between fiscal and monetary policy.
- We estimate that new measures announced since MYEFO will take around \$8.3bn off the government's bottom line over the next four years. These include relief measures following Cyclone Alfred and a boost to Medicare spending.
- On top of this we expect around \$8.3bn in additional measures to be announced. These will include an extension of last year's electricity rebates as well as enhancing Australia's capacity and supply chain resilience in renewables, batteries and critical minerals.
- The 2024/25 underlying cash deficit is estimated to be smaller at  $-0.9\%$  of GDP, compared to the December 2024 MYEFO estimate of  $1\%$  of GDP. However, despite the better-than-projected starting point, the budget deficit is still expected to widen over the coming three years.
- The RBA will take the Budget into account, but it is unlikely to shift the Bank's view on the outlook by much. We continue to expect three more rate cuts this year, bringing the policy rate to  $3.35\%$  by end-year.

## The big numbers

**SMALLER DEFICIT IN 2024-25,  
TEMPORARY AS DEFICITS SET TO  
WIDEN**

**2024-25: ( $-0.9\%$  GDP)**

**-\$25.8bn**

**2025-26: ( $-1.5\%$  GDP)**

**-\$44.0bn**

**NEW SPENDING OVER NEXT 4 YEARS:**

**\$16.6bn**

**2027-28: ( $-1.3\%$  GDP)**

**-\$33.9bn**

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# Budget 2025–26: Preview



**Sian Fenner**  
Head of Business & Industry Economics

The 2025/26 Budget will be handed down on Tuesday March 25 but is unlikely to contain any significant surprises. A number of pre-election measures have already been announced or flagged including.

- an \$8.5bn boost to Medicare spread over four years;
- \$1.2bn in disaster recovery and rebuilding in response to Cyclone Alfred;
- \$750m in support for the steel and aluminium industries following the US decision to raise tariffs by 25% on all aluminium and steel goods globally.
- a 20% haircut on student debt;
- increased defence spending and some infrastructure upgrades;
- various green industry support including the Green Iron Fund and Green Aluminium production credit.

However, many of these will only have a small impact on the underlying cash balance as they were either already included in the most recent MYEFO estimates or are 'off balance sheet' and/or impact beyond the Budget forecast horizon. We estimate that of the measures already announced, new spending amounts to around \$8.3bn over the next four years.

There are likely to be other announcements included in the Budget and as part of the election campaign but given the medium-term constraints on Australia's fiscal position, we expect any additional measures to be highly targeted and not a major 'cash splash'.

These will likely include targeted cost of living measures. With default electricity prices set to increase by between 2½ and 9%, depending on where people live, we look for last year's electricity rebates of \$300 for households and \$325 for SMEs to be extended to June 2026. We estimate that that this will cost around \$3.3bn. These measures could shave between 0.3–0.5ppts off headline CPI inflation although the RBA will again 'look through' these effects when assessing policy. Support for renewables, batteries and critical minerals is also expected to remain in focus with the Future Made in Australia initiative set to receive a boost.

## A \$1.1bn better starting point but still in deficit

We expect the Budget to revise its previous estimate for 2024/25 to a modestly smaller underlying cash deficit of -\$25.8bn or -0.9% of GDP for 2024/25 compared to the December 2024 MYEFO estimate of -\$27.0bn (-1% of GDP). The fiscal balance is estimated at -1.2% of GDP, lower than the -1.7% in MYEFO (Table 1).

Based on the Federal Government's financial statistics, which track budget outcomes against forecasts, the deficit for the first seven months to January 2025 was -\$30.7bn. This is an improvement versus the MYEFO profile of -\$40.7bn.

Most of this reflects an upward surprise in commodity prices and a lower exchange rate, which have boosted company tax receipts. A stronger labour market has also boosted tax revenue, whilst lowering payments. The ATO's increased focus on enforcing tax collection may also be bearing fruit. Nonetheless, the 2024/25 outcome will still mark a sharp turnaround in fortunes from an underlying cash surplus of \$15.8bn in 2023/24.

**Table 1: Key Fiscal Aggregates**

	2024/25		2025/26		2026/27		2027/28	
	MYEFO	Westpac	MYEFO	Westpac	MYEFO	Westpac	MYEFO	Westpac
Underlying cash balance \$bn	-27.0	-25.8	-46.9	-44.0	-38.4	-37.8	-31.7	-39.3
% of GDP	-1.0	-0.9	-1.6	-1.5	-1.3	-1.3	-1.0	-1.3
Fiscal balance %bn	-45.9	-33.8	-49.7	-52.2	-36.4	-45.8	-33.5	-47.3
% of GDP	-1.7	-1.2	-1.7	-1.8	-1.2	-1.5	-1.1	-1.5
Payments \$bn	704.2	706.0	728.4	735.9	763.4	765.3	804.1	796.3
% of GDP	25.5	25.5	25.5	25.7	25.4	25.9	25.4	25.9
Expenses \$bn	731.1	731.8	775.3	779.9	801.7	803.1	835.8	835.6
% of GDP	26.5	26.5	27.2	27.3	26.7	27.2	26.4	27.2

Sources: ABS, Budget papers, Westpac Economics

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## Large revenue surprises now firmly in the rear view mirror

We expect the fiscal boost, moderating inflation and lower interest rates to support firmer private demand over the coming year (see Appendix). The private sector will gradually take the baton of growth from the public sector, though this transition is likely to be bumpy and uneven. However, from a fiscal position it is the nominal side that matters.

On this front, Australia's commodity prices are easing amid slower global demand. Growth in nominal labour income is also expected to moderate as the labour market slows while net migration and population growth are also falling back. As inflation moderates we may also see the share of people with a second job fall from recent record highs<sup>1</sup>. Slower inflation also means multiple tax bases closely linked to price increases, such as GST collections, will expand more slowly.

Overall, nominal GDP growth is expected to decelerate to 1.3% in 2025/26, before increasing to 4.1% in 2027/28. This is lower than the MYEFO estimates of 3.5% and 5.5%. As such, even though Australia's tax take as a share of GDP will remain high, both historically and in an international context, revenue growth is projected to moderate and underperform MYEFO's estimates (Chart 1).

We also believe the scope for significant upward surprises to future revenues is more limited than in recent years. Indeed, on commodity prices, Treasury typically makes very cautious assumptions about the outlook for commodity prices, which has led to regular upside surprises to the Budget forecasts. For example, the price of iron ore is sitting at around US\$102 per tonne, while the assumed MYEFO glide path had prices at closer to US\$73 per tonne, falling to US\$60 per tonne by mid-2025 (Chart 2).

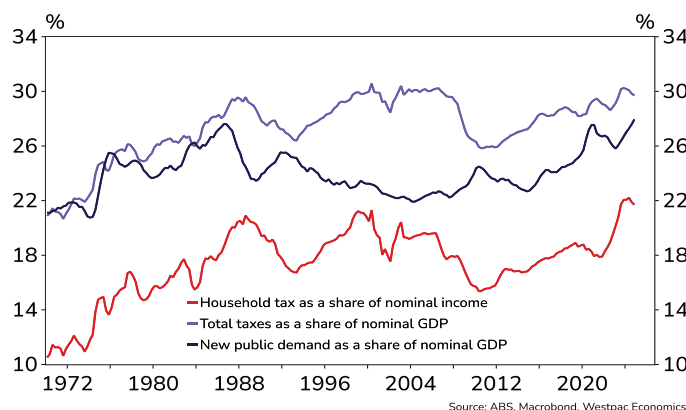
## Structural spending will increasingly offset the revenue base

Programs such as the NDIS, aged care and defence continue to expand. The 'care economy' – covering the government-dominated health, education and public admin sectors – now accounts for a record 27.8% of GDP. Ongoing demographic trends mean this sector will continue to place long-term pressure on the Budget (Chart 3). Off-budget spending also remains significant and is set to increase by around \$9bn, further straining government finances.

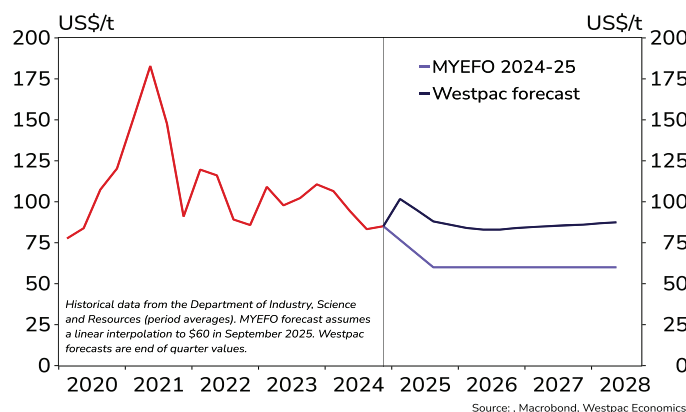
Consequently, despite the better starting point, the deficits are projected to widen significantly over the forecast horizon, to -\$39.3bn or 1.3% of GDP by 2027-28, with the fiscal deficit set to widen to 1.5% of GDP (Chart 4).

<sup>1</sup> This is known as the 'income effect', where labour rises/falls when real hourly wages falls/rises.

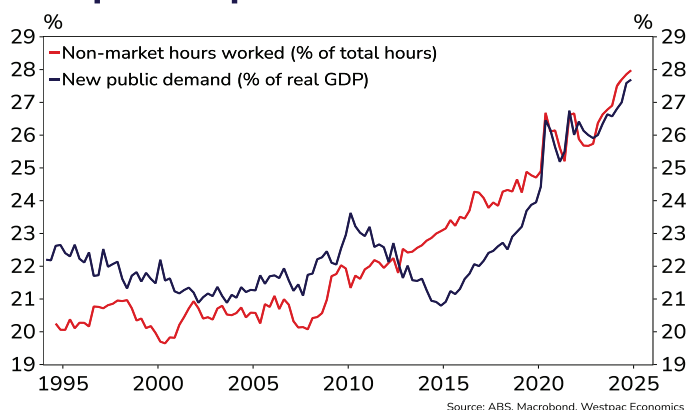
## Public demand and taxation relative to income



## Iron ore conservativeness low-balls revenue



## The expansion in public demand



## ... leading to higher borrowing and less fiscal space

Governments have already started to ramp up their borrowing even as taxes as a share of GDP are running at record highs and rising deficits will require further borrowing. Overall Australia's debt position is still lower than in most peer economies. Still, as debt escalates, there will be less fiscal space to implement counter-cyclical measures to help absorb future shocks, as they were able to for the GFC and the pandemic. This comes at a time when growing geopolitical uncertainty, increasing trade tensions, more frequent weather events and ongoing technological change may mean shocks are more frequent.

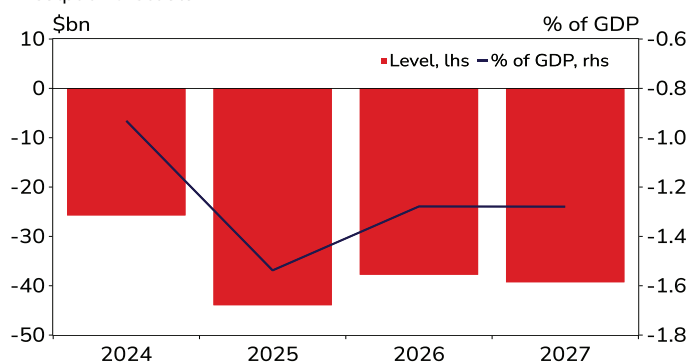
## RBA reaction

The RBA will take the Budget into account, but it is unlikely to shift its view on the outlook by much. The RBA delivered a hawkish 25bp cut in February and based on RBA staff economic projections it would be reasonable to assume one more rate cut this year.

Our own forecasts differ somewhat: we expect a bit more easing in the labour market and a more gradual pick-up in consumption, leading to a bit more of a decline in inflation. These differences are small but on net are enough that we look for a further three rate cuts this year, bringing the policy rate to 3.35% by end-year. This is predicated on the economy turning out in line with our own forecasts.

## Underlying Cash Balance

Westpac Forecasts



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

# Australian Economic Forecasts (March 2025 Market Outlook)

## Activity forecasts\*

	2024		2025				2026		Calendar years			
%qtr / %yr avg	Q3	Q4	Q1f	Q2f	Q3f	Q4f	Q1f	Q2f	2023	2024	2025f	2026f
Private consumption	-0.1	0.4	0.3	0.5	0.5	0.5	0.6	0.6	2.5	0.6	1.3	2.2
Dwelling investment	1.5	-0.4	1.5	1.5	1.2	1.2	1.3	1.6	-1.3	-0.4	4.2	5.8
Business investment **	-0.4	0.5	0.6	0.7	0.8	0.9	1.1	1.2	8.3	2.5	2.0	4.4
Private demand **	0.0	0.4	0.5	0.6	0.6	0.6	0.7	0.8	2.8	1.0	1.7	3.0
Public demand **	2.5	1.0	0.8	0.7	0.9	0.7	0.7	0.6	3.1	4.4	4.1	2.7
Domestic demand	0.7	0.5	0.5	0.7	0.7	0.6	0.7	0.7	2.9	1.9	2.4	2.9
Stock contribution	-0.3	0.1	0.0	0.0	0.0	0.0	0.1	0.1	-1.0	0.1	-0.2	0.2
GNE	0.4	0.6	0.5	0.7	0.7	0.7	0.8	0.8	1.9	2.0	2.2	3.1
Exports	0.2	0.7	0.5	0.4	0.3	0.4	0.4	0.4	6.9	0.9	1.8	1.5
Imports	-0.2	0.1	0.7	0.7	0.7	0.9	1.5	1.6	6.8	5.5	1.9	5.0
Net exports contribution	0.1	0.2	0.0	-0.1	-0.1	-0.1	-0.3	-0.3	0.3	-1.0	0.0	-0.8
<b>Real GDP %qtr / yr avg</b>	<b>0.3</b>	<b>0.6</b>	<b>0.5</b>	<b>0.6</b>	<b>0.6</b>	<b>0.5</b>	<b>0.5</b>	<b>0.5</b>	<b>2.1</b>	<b>1.0</b>	<b>2.0</b>	<b>2.2</b>
<b>%yr end</b>	<b>0.8</b>	<b>1.3</b>	<b>1.6</b>	<b>2.0</b>	<b>2.3</b>	<b>2.2</b>	<b>2.2</b>	<b>2.2</b>	<b>1.5</b>	<b>1.3</b>	<b>2.2</b>	<b>2.2</b>
Nominal GDP %qtr	0.5	1.6	0.6	0.8	1.0	0.7	0.7	0.8	-	-	-	-
%yr end	3.5	3.7	3.0	3.6	4.0	3.1	3.2	3.2	4.3	3.7	3.1	3.3

## Other macroeconomic variables

	2024		2025				2026		Calendar years			
% change	Q3	Q4	Q1f	Q2f	Q3f	Q4f	Q1f	Q2f	2023	2024	2025f	2026f
Employment (2)	0.9	0.7	0.8	0.1	0.0	0.0	0.2	0.2	-	-	-	-
%yr	2.7	2.7	3.2	2.7	1.7	1.0	0.4	0.5	3.0	2.7	1.0	1.2
Unemployment rate % (2)	4.1	4.0	4.1	4.2	4.4	4.5	4.5	4.5	3.9	4.0	4.5	4.5
Wages (WPI) (sa) (2)	0.9	0.7	0.8	0.7	0.7	0.7	0.8	0.8	-	-	-	-
annual chg	3.6	3.2	3.2	3.0	2.9	2.9	3.0	3.1	4.2	3.2	2.9	3.3
CPI Headline (2)	0.2	0.2	0.7	0.9	0.9	0.6	0.6	0.8	-	-	-	-
annual chg	2.8	2.4	2.2	2.0	2.7	3.2	3.1	3.0	4.1	2.4	3.2	2.7
Trimmed mean	0.8	0.5	0.5	0.6	0.7	0.7	0.6	0.6	-	-	-	-
annual chg	3.6	3.2	2.7	2.4	2.3	2.5	2.6	2.6	4.2	3.2	2.5	2.5
Current account \$bn	-13.9	-12.5	-12.8	-13.6	-13.9	-14.4	-16.6	-18.1	-	-	-	-
% of GDP	-2.0	-1.8	-1.8	-1.9	-2.0	-2.0	-2.3	-2.5	-0.2	-1.8	-2.0	-2.8
Terms of trade annual chg (1)	-4.7	-4.8	-4.3	-4.1	-3.4	-3.1	-2.6	-2.7	-6.2	-4.8	-3.1	-2.8

Calendar year changes are (1) period average for GDP, terms of trade, unless otherwise stated (2) through the year for inflation, wages and employment. Unemployment is year end.

\* GDP & component forecasts are reviewed following the release of quarterly national accounts.

\*\* Business investment and government spending adjusted to exclude the effect of private sector purchases of public sector assets.



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