

PART 1: OVERVIEW

The Government is focused on building a stronger economy to drive further gains in employment and prosperity. The 2015-16 Mid-Year Economic and Fiscal Outlook (MYEFO) shows the Government's fiscal position is forecast to maintain an improving trajectory over the forward estimates period, despite changes in economic parameters detracting from the fiscal outlook since the 2015-16 Budget.

The Australian economy continues to perform well, transitioning from strong resource investment-led growth to broader-based drivers of economic activity. Employment growth has strengthened as the economy transitions to more labour intensive sectors. While business investment intentions currently remain subdued, conditions conducive to stronger business investment are in place.

Building on Australia's economic growth record requires sound government finances, continued investment in Australia's productive capacity and policy settings that support the innovation and drive of Australian workers and businesses. This underscores the importance of the Government's integrated national plan for economic growth and jobs.

UPDATED FISCAL OUTLOOK

The underlying cash deficit is expected to narrow from \$37.4 billion (2.3 per cent of GDP) in 2015-16 to \$14.2 billion (0.7 per cent of GDP) in 2018-19. The average annual pace of fiscal consolidation is 0.4 per cent of GDP over the forward estimates period, only slightly less than the 2015-16 Budget despite economic parameter variations detracting significantly from the fiscal outlook.

Table 1.1: Budget aggregates

	Estimates			
	2015-16		2016-17	
	Budget	MYEFO	Budget	MYEFO
Underlying cash balance(\$b)(a)	-35.1	-37.4	-25.8	-33.7
Per cent of GDP	-2.1	-2.3	-1.5	-2.0
Fiscal balance(\$b)	-33.0	-35.8	-23.4	-32.8
Per cent of GDP	-2.0	-2.2	-1.3	-1.9
	Projections			
	2017-18		2018-19	
	Budget	MYEFO	Budget	MYEFO
Underlying cash balance(\$b)(a)	-14.4	-23.0	-6.9	-14.2
Per cent of GDP	-0.8	-1.3	-0.4	-0.7
Fiscal balance(\$b)	-9.2	-17.4	-3.2	-10.2
Per cent of GDP	-0.5	-1.0	-0.2	-0.5

(a) Excludes expected net Future Fund earnings.

Net debt is projected to peak at 18.5 per cent of GDP in 2017-18 and then decline over the medium term.

Part 1: Overview

Government payments as a share of GDP are expected to decline from 25.9 per cent of GDP in 2015-16 to 25.3 per cent of GDP in 2018-19. Based on the 2014-15 Budget outcome, real growth in payments over the forward estimates has fallen since the 2015-16 Budget from 2.0 per cent to 1.8 per cent due to a lower spending profile.

Consistent with the Government's fiscal strategy, spending decisions taken since the 2015-16 Budget, including those arising from Senate negotiations, have been more than offset by reductions in spending elsewhere in the budget. After taking into account the provision previously made for the China-Australia Free Trade Agreement, new policy decisions taken since the 2015-16 Budget have had a positive net impact on the underlying cash balance over the forward estimates (see Table 3.6).

Excluding policy changes, total receipts are expected to be \$33.8 billion lower over the forward estimates than expected at the 2015-16 Budget. This largely reflects revisions to forecast nominal GDP, with declining commodity prices resulting in lower company tax receipts and a weaker outlook for wages and population growth, leading to lower expected income tax from individuals. Furthermore, weaker equity markets since the 2015-16 Budget have also resulted in downward revisions to receipts from capital gains tax.

Partly offsetting the impact of lower forecast tax receipts, stronger employment and slower population growth have driven a decrease in expected personal benefit payments.

UPDATED ECONOMIC OUTLOOK

The Australian economy continues to perform well. Australia's real GDP growth is forecast to strengthen from 2½ per cent in 2015-16 to 2¾ per cent in 2016-17, with the economy's transition from resource investment-led growth towards broader-based drivers of activity appearing to be underway. This transition is being supported by historically low interest rates, the fall in the Australian dollar and lower oil prices.

World economic growth is expected to improve in 2016 and 2017, providing support to Australia's growth outlook. Global conditions remain uneven, with significant divergence across the major advanced economies. Growth in emerging market economies is expected to pick up in 2016 and 2017, driving more than 70 per cent of world growth. However, risks to the global outlook remain elevated, with China's shifting composition of growth and an uncertain market reaction to the withdrawal of monetary policy stimulus in the United States raising the potential for further volatility.

The Treasury has updated its technical assumptions for growth in the working-age population and average hours worked, which has affected estimates of the economy's potential output. This contributes to lower projected growth in real and nominal GDP over the coming years.

The assumed pace of real GDP growth in the five years from 2017-18 has been revised down to 3 per cent, from the 3½ per cent assumed in the 2014-15 Budget.

Changes to the economic assumptions underpinning the projections have reduced the projected underlying cash balance by around \$9 billion over the forward estimates. These changes also affect the medium-term fiscal projections, with weaker tax receipts impacting the return to surplus (see Box A in Part 3).

Table 1.2: Major economic parameters^(a)

	Outcomes	Forecasts		Projections	
	2014-15	2015-16	2016-17	2017-18	2018-19
Real GDP	2.2	2 1/2	2 3/4	3	3
Employment	1.5	2	1 3/4	1 1/2	1 1/2
Unemployment rate	6.0	6	6	5 3/4	5 1/2
Consumer price index	1.5	2	2 1/4	2 1/2	2 1/2
Wage price index	2.3	2 1/2	2 3/4	2 3/4	3
Nominal GDP	1.6	2 3/4	4 1/2	5	5 1/4

(a) Year average unless otherwise stated. From 2014-15 to 2016-17, employment and the wage price index are through the year growth to the June quarter. The unemployment rate is the rate for the June quarter. The consumer price index is through the year growth to the June quarter.

Source: Treasury projections.

The number of Australians with jobs rose by over 340,000 over the past year. Employment is forecast to grow by 2 per cent through the year to the June quarter of 2016 and by 1¾ per cent to the June quarter of 2017. The unemployment rate is expected to peak at a lower level than previously forecast, remaining at around 6 per cent in the June quarters of 2016 and 2017.

Soft commodity prices and a moderate outlook for inflation and wages are expected to weigh on nominal GDP growth over the forecast period. Forecast nominal GDP growth has been revised down since the 2015-16 Budget to 2¾ per cent in 2015-16 and 4½ per cent in 2016-17.

The iron ore price assumption has been reduced from US\$48 per tonne at the 2015-16 Budget to US\$39 per tonne. While the depreciation of the Australian dollar provides some buffer, the fall in prices is expected to detract around \$7 billion from forecast tax receipts over the forward estimates.

Moderate income growth highlights the importance of improving Australia's productivity performance to support future growth in national living standards.

A NATIONAL PLAN FOR ECONOMIC GROWTH AND JOBS

The Government is investing in the drivers of Australia's future prosperity and supporting job creation through its integrated national plan for economic growth and jobs. The Government is putting in place policies to create a dynamic, competitive economy that rewards effort, incentivises innovation and sets Australia up to capitalise on the abundant opportunities in the fast-growing Asian region.

The Government's National Innovation and Science Agenda backs Australians to generate and capitalise on ideas that will grow the economy and create jobs. Encouraging innovation is a key part of the Government's strategy to build a stronger, more competitive and more dynamic economy.

Complementing this agenda, free trade agreements with China, Japan and Korea and the historic Trans-Pacific Partnership Agreement (TPP) will open up new trade opportunities in the rapidly growing Asia Pacific region. The trade and investment guaranteed by the Government's trade deals with regional partners will support growth, job creation and income for Australia.

The Government is supporting record levels of infrastructure investment through its \$50 billion infrastructure package, increasing the economy's productive capacity, creating jobs and expanding business and labour market opportunities. As part of this, the Government is partnering with the States and Territories to release capital to fund productive infrastructure through the Asset Recycling Initiative.

The Government's response to the Financial System Inquiry will further strengthen Australia's already robust financial system by ensuring it continues to meet the needs of Australians and supports sustainable growth in the economy.

The Government is also strengthening Australia's competition frameworks through its response to the Harper Review to support a more dynamic, productive and innovative economy and improve living standards. This includes working with the State and Territory governments to unlock the benefits of choice and diversity in areas such as health and aged care.

The Government has initiated a comprehensive dialogue on how to create a 'growth friendly' tax system that backs Australians who are working, saving and investing. As demonstrated by the National Innovation and Science Agenda, the Government's focus is on changes to the tax system that will help grow our economy and create jobs, while ensuring the burden of taxation is fair.

A strengthening budget position is another important pillar of a strong, resilient economy. As the 2015-16 MYEFO shows, the Government's policies and continued fiscal control maintain an improving trajectory for the budget position despite global economic headwinds.