Federal Budget in Brief
2022-23 October Budget
NAB Group Economics

Summary

The new budget's announcements are broadly in line with media reporting over recent days and mostly reflect a number of election commitments. A deficit of $37bn is forecast for 2022/23 (down from an expected $80bn as recently as April), widening slightly over the out years as temporary revenue gains fade. Cumulatively, the deficit is $43bn smaller over the next 4 years, resulting in a slightly lower debt burden over the forward estimates as compared to the Pre-election Economic and Fiscal Outlook (PEFO).

Key policy changes were largely confined to the Government's election promises including expanded childcare subsidies ($4.7b), aged care reforms ($2.5b), university and vocational education places ($1.4b) and lowering prescription costs ($0.8b). There were also new announcements on parental leave ($0.5b) and affordable housing ($0.4b). The Budget also includes $8.1b over 10 years for infrastructure and additional investments in the NBN, energy transmission, and social housing. The impact of higher indexation for welfare and growing NDIS costs are also noted, in addition to a rise in debt servicing costs.

While this budget does little to address medium-term structural budget issues, it does lay the groundwork for the government to seek to address these challenges more actively in the future. The budget highlights that the better-than-expected outcomes in both 2022/23 and 2023/24 resulted in large part from higher commodity prices and large employment and wage gains. These impacts are expected to wane and, in the medium-term, slower assumed trend growth and rising NDIS and debt servicing costs see the budget projected to remain in deficit well beyond 2030.

Importantly, however, in the context of high inflation our estimates suggest the fiscal impact on growth is neutral over the next two years. In the absence of a significant structural tightening, monetary policy will likely remain the key tool in moderating demand and inflationary pressure in the near term, pointing to some upside risk on our rates profile.

Economic outlook

Overall, the patterns in our key domestic macro forecasts and the budget are fairly similar. Overall growth is expected to slow to below trend rates of around 1.6% in 2023/24 in year-average terms (Budget: 1.5% from 2.5% at PEFO) after a very strong 3.4% in the current financial year (Budget: 3.25% from 3.5%). Unemployment is expected to rise moderately (but broadly consistent with full employment) and inflation to remain elevated in the near-term before easing back into the RBA's target band in 2024. In terms of risks, we share similar concerns to the budget papers, with global uncertainty remaining high as well as the potential for rates to rise further domestically depending on the inflation path and consumers' reaction to higher rates and inflation in the near-term.

Fiscal & Debt Outlook

The deficit for 2022/23 is expected to be $37b or 1.5% of GDP ($78b or 3.4% of GDP at PEFO). The deficit is forecast to widen marginally to $44.0b (1.8% of GDP) in 2023/24, $51.3b (2.0% of GDP) in 2024/25 and $49.6b (1.8% of GDP) in 2025/26. The cumulative improvement over the forward estimates totals $43bn compared to PEFO. Gross debt is forecast to stabilise at 46.9% of GDP in 2030/31, while net debt is forecast to reach 31.9% of GDP in 2033 (the end of the projection period).

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Economic Outlook and Forecast Comparison

Global Context and Forecasts

Global growth has slowed this year and we expect a further significant slowing in 2023. Rapid monetary policy tightening and the energy supply shock caused by Russia's invasion of Ukraine are likely to see the US, UK, and Euro-zone enter into at least mild recessions, which will have spill over impacts to other countries. China's zero-COVID-19 policy will continue to disrupt its economy while it remains in place, and a downturn in its property sector is an additional headwind.

The October Budget (Treasury) forecasts also see a slowdown in global growth, though their global forecast is more optimistic than ours in both 2023 and 2024 – largely reflecting stronger growth expectations for advanced economies as well as India. However, Treasury's forecast for major trading partner growth is slightly weaker than ours in 2023. Overall, forecast uncertainty in the current environment is particularly elevated, and they are broadly in-line with the IMF's forecasts released earlier this month.

Australian Outlook and Forecasts

Overall, the patterns between our key domestic macro forecasts and the Treasury's forecasts are fairly similar. Overall growth is expected to slow to below trend rates of around 1.6% in 2023/24 in year-average terms (Budget: 1.5%) after a very strong 3.4% in the current financial year (Budget: 3.25%). Unemployment is expected to rise moderately (but still consistent with full employment) and inflation to remain elevated in the near-term before easing back into the RBA's target band in 2024.

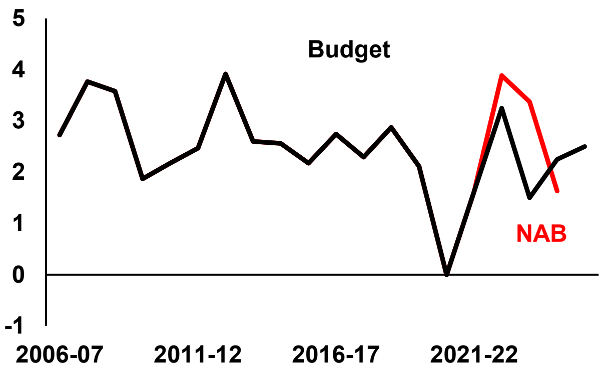
On growth, we expect the slowing to come through softer household consumption growth as the impact of higher interest rates and inflation weighs on disposable incomes. Business investment is expected to make a small contribution to growth, supported by strong trading conditions, high capacity utilisation and elevated capex intentions. Dwelling investment should remain elevated but will likely be volatile on a quarterly basis with a large pipeline of work disrupted by the availability of labour and materials. Activity should eventually ease as the pipeline of work is completed. Government spending will grow more slowly but also remain high.

As growth slows to well-below trend rates, both we and the Treasury expect the unemployment rate to rise to around 4.3% (Budget: 4.5%) as labour demand cools and population growth accelerates. That said, the unemployment rate remains broadly consistent with the NAIRU in the near term. This is important for wage growth. which is in turn significant for the revenue side of the budget. We see wage growth accelerating to around 3.5% by next year (Budget: 3.75%). Further out the budget assumes wage growth slows to around 3.5% as labour constraints ease.

Table 1: Treasury vs NAB Forecasts, Key Economies

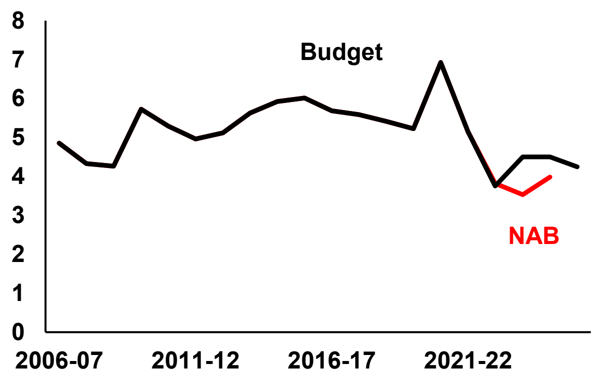
Comparison of Treasury Budget Forecasts and NAB Forecasts	2022		2023		2024	
	Treasury	NAB	Treasury	NAB	Treasury	NAB
US	1.8	1.8	1.0	0.0	1.8	1.1
Euro-zone	3.0	3.2	0.5	0.0	1.5	1.1
Japan	1.5	1.6	1.5	1.4	1.0	0.9
China	3.0	3.4	4.5	5.0	4.5	4.5
India	7.3	7.3	5.8	4.4	6.8	5.6
Other East Asia	4.5	4.5	4.0	3.3	4.3	3.7
World	3.0	3.2	2.8	2.3	3.0	2.8
Major trading partners	3.0	3.5	3.0	3.4	3.3	3.4

Chart 1: Real GDP Growth Forecast Comparison (%)



Source: Commonwealth Treasury.

Chart 2: Unemployment Rate Forecast Comparison (%)



Source: Commonwealth Treasury.

As global inflationary pressures fade, domestic pressures will become relatively more important, though our estimates for wage growth are not inconsistent with at-target inflation. We do see a faster moderation in headline inflation than Treasury over the next two years, but see a similar end point around 2.5% near the end of 2025.

Treasury has incorporated a conservative outlook for commodity prices with metal ores and thermal coal which return rapidly to their long run average. This appears fair in the context of global risks while managing the budget outlook. Energy prices (as noted in the budget itself) may see some upside risk.

Of note, Treasury has revised its estimate of long term potential growth on the back of a softer productivity assumption, bringing the budget assumption of 2.5% closer to our working estimate of 2.25-2.5%.

Budget Position and Fiscal Impulse

Summary of Key Budget Metrics

The October Budget estimates that there will be an underlying cash deficit of $36.9b (1.5% of GDP) in 2022-23. This represents a $41b (1.9% of GDP) improvement on the Pre-election Economic and Fiscal Outlook (PEFO) estimate reflecting much higher receipts than previously expected, which more than offset an increase in payments. However, the deficit is only $12.5b lower in 2023-24 than in the PEFO and, on average, $5.5b higher over 2024-25 and 2025-26.

As a result, the previous profile of an improving trend in the underlying cash deficit over time has been replaced with one where the deficit is lower to start with but rises out to 2024-25 (both in dollar terms and as a % of GDP) before stabilising.

As a percent of GDP, both revenue and expenses are expected to decline in 2022-23, although this reflects the larger-than-expected growth in nominal GDP (with both revenue and expenses, in dollar terms, growing by over 4%). Beyond 2022-23, revenue (% of GDP) is expected to remain broadly unchanged, but there is upwards pressure on expenses.

The Budget papers present an allocation of the changes in the Budget outlook, relative to PEFO, between 'parameter' adjustments and policy decisions. Parameter adjustments include, for example, differences in program take up rates, or the impact on revenue from revisions to the economic outlook.

Parameter adjustments are a positive factor in 2022-23 and 2023-24 but then turn almost neutral (as both higher payments and receipts in the final two years net out). This reflects a large initial boost to receipts in 2022-23 which dissipates somewhat in remaining years, in part due to an assumed fall in commodity prices. In contrast, the upward revision to payments due to parameters climbs over time. The latter reflects higher rates of indexation (to either CPI or wages) for various programs, rising interest costs, and higher expected NDIS participants (and costs per plan).

In contrast, the impact of policy changes is relatively minor in both 2022-23 and 2023-24 but starts to lift in 2024-25 and by even more into 2025-26.

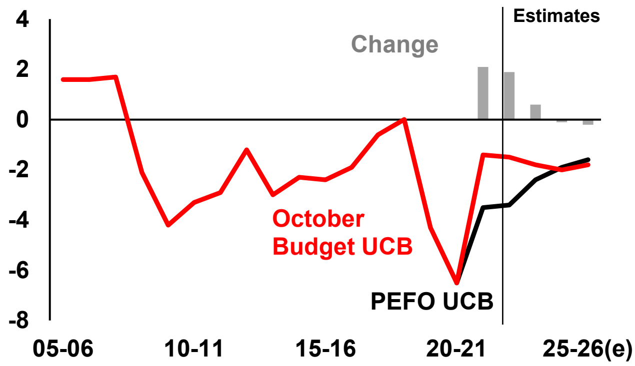
In essence the October Budget projects that the recent gains in the budget position reflect factors which will be transitory as the economy slows and commodity prices fall, and that the costs of running existing program (such as NDIS) and in servicing government debt are rising.

Table 2: Key Budget Metrics

	2021-22	2022-23(e)	2023-24(e)	2024-25(e)	2025-26(e)
UCB, $bn	-32.0	-36.9	-44.0	-51.3	-49.6
% of GDP	*-1.4*	*-1.5*	*-1.8*	*-2.0*	*-1.8*
Net op. bal., $bn	-26.6	-25.9	-33.0	-53.2	-40.0
% of GDP	*-1.2*	*-1.0*	*-1.3*	*-2.1*	*-1.5*
Net cptl. inv. $bn	8.4	12.8	11.9	9.0	9.9
% of GDP	*0.4*	*0.5*	*0.5*	*0.4*	*0.4*
Fiscal bal., $bn	-35.1	-38.7	-44.9	-62.1	-49.9
% of GDP	*-1.5*	*-1.6*	*-1.8*	*-2.4*	*-1.9*
Net debt, $bn	515.7	572.2	634.1	702.8	766.8
% of GDP	*22.5*	*23.0*	*25.8*	*27.4*	*28.5*

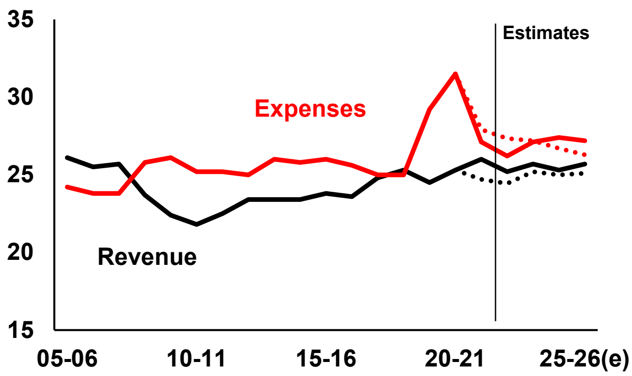
Source: Commonwealth Treasury.

Chart 3: Underlying Cash Balance (UCB) (% of GDP)



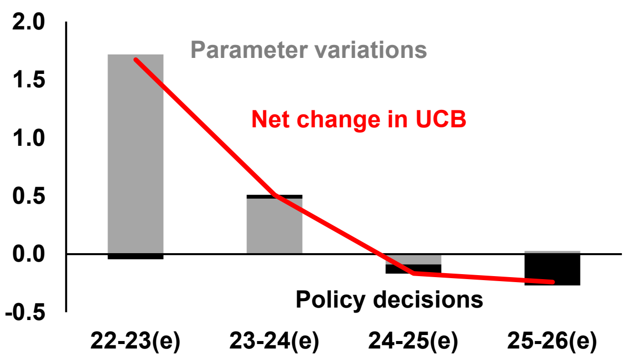
Source: Commonwealth Treasury.

Chart 4: Govt Revenue & Expenses (% of GDP)



Dotted lines show PEFO. Solid lines show October Budget. Source: Commonwealth Treasury.

Chart 5: Reasons for Change in UCB (% GDP)*



Source: Commonwealth Treasury. * Change beteen October 2022-23 Budget and PEFO

Estimated Fiscal Impulse

The small net amount of policy changes suggests a largely neutral impact on the outlook for the economy from this budget (over and above the normal 'automatic stabilisers' from program outlays, or changes in revenue, as the economy changes).

Another way to look at the macroeconomic impact of the Budget is, as we have done in the past, to estimate the structural changes of Budget measures by excluding the (estimated) influence of cyclical factors. That is, what the Budget is doing to the economy as opposed to what the economy is doing to the Budget.

The change in the estimated structural budget balance from year-to-year – the 'fiscal impulse' – provides an indication of the Budget's macroeconomic impact (Chart 8). Unsurprisingly, the fiscal impulse measure suggests policy was highly stimulative in 2019-20 and 2020-21 due to the COVID-19 policy response. The fiscal impulse was negative in 2021-22 as COVID-19 related programs ended or scaled down. For 2022-23 and beyond there is little fiscal impulse in either direction – i.e. the Budget is basically having a neutral economic impact. This contrasts somewhat to the fiscal impulse estimates at the time of the March Budget, which suggested some (but not major) tightening in policy.

The precision of any fiscal impulse estimate shouldn't be overstated, but what this analysis does suggest is that the task of reducing demand pressures in the economy is, at this stage, being left to the RBA.

Government Debt and Outlook for the Medium Term

Reflecting the significant improvement in the underlying cash balance for 2021-22 and 2022-23, and the rise in bond yields (which reduce the market value of Government securities (AGS) on issue) the net debt profile has been lowered compared to the March Budget over the forward estimates. The reduction in the gross debt profile – which is based on the face value of AGS and so not affected in the same way by changes in interest rates – is smaller.

Over the medium term, borrowing costs are expected to be higher and the cost of the NDIS is expected to grow more quickly than previously forecast. The government has also adopted a revised long-run productivity growth assumption of 1.2%, in line with the 20-year average (down from the 1.5% 30-year average used in past budgets).

These factors have contributed to a deterioration relative to PEFO, with the underlying cash balance projected to remain in a deficit of around 2% of GDP to 2032-33. Gross debt is expected to stabilize at around 46.9% of GDP in 2031-32, while net debt is expected to reach 31.9% of GDP in June 2033 (the end of the projection period). The Budget highlights that while debt is projected to be higher

Chart 6: Structural Fiscal Impulse Estimates

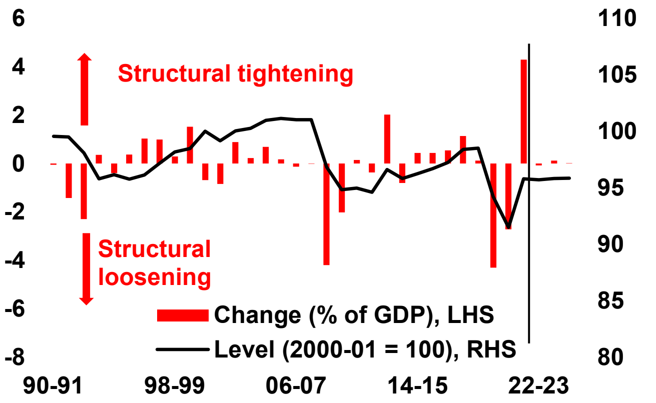
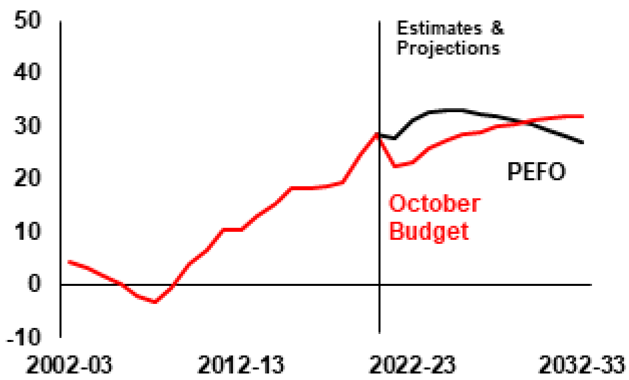
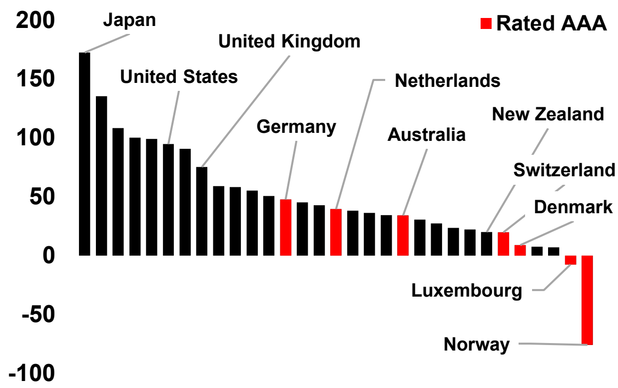


Chart 7: Fed. Government Net Debt (% GDP)



Source: Commonwealth Treasury.

Chart 8: Govt Debt, Advanced Economies, 2022 (% GDP)



Source: IMF World Economic Outlook.

than at PEFO, it is lower than the level that would have been projected at PEFO under the same assumptions.

These levels of debt are high by Australian Federal government standards, but internationally, in terms of total government debt, Australia remains a low debt country. While Australian government debt has increased since the start of the pandemic, this has also been the case in many other countries. Nonetheless, the revised projections in the Budget including the use of a revised productivity growth assumption highlight the considerable structural fiscal challenge that remains for the government.

Key Policy Measures

Childcare

$4.7 billion over 4 years from 2022-23 to lower the cost of childcare. This includes increasing the maximum Child Care Subsidy (CCS) rate from 85% to 90% and increasing the CCS rate for all households earning less than $530,000 in income.

Aged care

$2.5 billion over 4 years from 2022–23 to support reform in the aged care sector. The bulk of funding will ensure all residential aged care facilities have a registered nurse on duty 24 hours a day from 1 July 2023 and increasing care minutes per resident per day from 1 October 2024.

A further $540.3 million over 4 years from 2022–23 to improve service delivery, in response to the Royal Commission into Aged Care Quality and Safety, including investments in information and communications technology.

Vocational education

$871.7 million over 5 years from 2022–23 to provide 480,000 fee-free TAFE places, with a specific focus on industries and regions identified with skills shortages.

And additional $50 million over 2 years from 2022-23 to modernise TAFE facilities.

Prescription medicines

$787.1 million over 4 years to reduce the maximum co-payments for medicines under the Pharmaceutical Benefits Scheme (PBS) from $42.50 per script to $30 per script.

$1.4 billion over 4 years from 2022–23 for new and amended listings on the PBS, the Repatriation Pharmaceutical Benefits Scheme, the Life Saving Drugs Program, the National Diabetes Services Scheme and the Stoma Appliance Scheme.

Paid parental leave

$531.6 million over 4 years to expand paid parental leave to 26 weeks by 2026 (currently 18 weeks paid parental leave and two weeks of secondary carer leave). Parents will be able to divide the leave between themselves, as well as taking leave in blocks as small as individual days.

Affordable housing

$350.0 million over 5 years from 2024–25 to support funding of an additional 10,000 affordable homes. This would come under a Housing Accord with state and territory governments and other key stakeholders (such as investors – particularly from the superannuation sector – and the construction industry).

The Government will also invest $10 billion in the Housing Australia Future Fund. Returns from this investment will fund 30,000 social and affordable homes over 5 years.

Universities

$485.5 million over 4 years from 2022–23 to provide an additional 20,000 Commonwealth supported places at universities and other higher education providers starting in 2023 and 2024. These places will be for under-represented segments of the community, in courses with identified skills shortages, such as teaching, nursing and engineering.

National Anti-Corruption Commission

$262.6 million over 4 years from 2022–23 to establish and support the ongoing operation of the National Anti-Corruption Commission.

Electric vehicles tax reduction

Reduced taxes to encourage the uptake of electric vehicles will cost $345 million over 4 years from 2022–23.

Infrastructure

An additional $8.1 billion over 10 years from 2022–23 for priority rail and road infrastructure projects across Australia, including the Suburban Rail Loop in Victoria, the Bruce Highway, Inland Freight Route, Beef Corridors and Kuranda Range Road in Queensland, planning and early works for the Sydney to Newcastle High Speed Rail and New England Highway – Muswellbrook Bypass in NSW.

The Government will also provide an equity investment of $2.4 billion over 4 years from 2022-23 to NBN Co to increase optic fibre internet access to an additional 1.5 million premises by 2025.

The Government will also provide $20 billion in funding to establish Rewiring the Nation, a fund that will provide concessional loans and equity to support investment in expanding and modernising Australia's electricity grids and storage (to support growth of renewables).

Savings will be generated by the cancellation of various previously committed infrastructure projects.

Appendix: Detailed Fiscal and Economic Tables

Table 3: Key Budget Metrics, October Budget vs March Budget 2022-23

	2021-22		2022-23(e)		2023-24(e)		2024-25(e)		2025-26(e)	
	PEFO	October Budget	PEFO	October Budget	PEFO	October Budget	PEFO	October Budget	PEFO	October Budget
Underlying cash balance, $bn	-79.8	-32.0	-77.9	-36.9	-56.5	-44.0	-47.1	-51.3	-42.9	-49.6
% of GDP	*-3.5*	*-1.4*	*-3.4*	*-1.5*	*-2.4*	*-1.8*	*-1.9*	*-2.0*	*-1.6*	*-1.8*
Net operating balance, $bn	-73.4	-26.6	-67.2	-25.9	-48.2	-33.0	-43.6	-53.2	-31.5	-40.0
% of GDP	*-3.2*	*-1.2*	*-2.9*	*-1.0*	*-2.0*	*-1.3*	*-1.8*	*-2.1*	*-1.2*	*-1.5*
Net capital investment, $bn *	11.1	8.4	11.3	12.8	10.6	11.9	7.4	9.0	8.2	9.9
% of GDP	*0.5*	*0.4*	*0.5*	*0.5*	*0.4*	*0.5*	*0.3*	*0.4*	*0.3*	*0.4*
Fiscal balance, $bn	-84.6	-35.1	-78.6	-38.7	-58.4	-44.9	-51.1	-62.1	-39.6	-49.9
% of GDP	*-3.7*	*-1.5*	*-3.4*	*-1.6*	*-2.5*	*-1.8*	*-2.1*	*-2.4*	*-1.5*	*-1.9*
Net debt, $bn	631.5	515.7	714.9	572.2	772.1	634.1	823.2	702.8	864.5	766.8
% of GDP	*27.6*	*22.5*	*31.1*	*23.0*	*32.6*	*25.8*	*33.1*	*27.4*	*33.1*	*28.5*

Table 4: Economic Forecasts, Treasury vs NAB

	2021-22	2022-23(f)		2023-24(f)		2024-25(f)		2025-26(f)	
	Outcome	Budget	NAB	Budget	NAB	Budget	NAB	Budget	NAB
GDP and Components									
Private Consumption	4.1	6 1/2	6.6	1 1/4	1.8				
Dwelling Investment	2.8	-2	-1.5	-1	0.5				
Underlying Business Investment	4.8	6	2.9	3.5	2.5				
Underlying Public Final Demand	6.8	1	2.7	1 1/2	2.1				
Domestic Demand	**5.1**	**n/a**	**4.3**	**n/a**	**1.9**				
Stocks (Cont. to GDP)	0.1	0	-0.2	- 1/4	0.0				
Gross National Expenditure	**5.2**	**4**	**4.1**	**1**	**1.8**				
Exports	0.0	7	6.0	5	2.5				
Imports	7.7	11	9.3	3	3.2				
Net Export (Cont. to GDP)	-0.9	- 3/4	-0.1	1/2	-0.2				
Real GDP	**3.9**	**3 1/4**	**3.4**	**1 1/2**	**1.6**	**2 1/4**	**n.a.**	**2 1/2**	**n.a.**
Nominal GDP	11.1	8	9.6	-1	3.3	4.25	n.a.	5	n.a.
External Account									
Current Account Balance ($b)	50.0	n.a.	52.3	n.a.	9.5				
Current Account Balance (% of GDP)	2.2	1/2	2.1	-3 3/4	0.4				
Terms of Trade	12.1	-2.5	1.6	-20	-6.0				
Labour Market									
Employment (Yr-ended)	3.1	1 3/4	2.2	3/4	1.1	1	n.a.	1.25	n.a.
Unemployment Rate (End of period)	3.8	3.75	3.5	4 1/2	4.0	4 1/2	n.a.	4 1/4	n.a.
Wage Price Index (WPI) (Yr-ended)	2.6	3 3/4	3.5	3 3/4	3.4	3 1/4	n.a.	3 1/2	n.a.
Prices and Rates									
Headline CPI (Yr-ended)	6.1	5 3/4	4.9	3 1/2	2.6	2 1/2	n.a.	2 1/2	n.a.
Trimmed-mean CPI (Yr-ended)	4.9	n.a.	4.9	n.a.	3.0				
RBA Cash Rate (End of period)	0.85	n.a.	3.10	n.a.	3.10				
10 Year Govt. Bonds (End of period)	3.69	n.a.	4.05	n.a.	3.65				
$A/US cents (End of period)	0.69	n.a.	0.70	n.a.	0.72				

Data are annual average percentage growth, except where specified otherwise.
Source: Commonwealth Treasury and NAB Economics.

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Important notice