

The 2009 May Federal Budget Economic Fact or Fiction

In the Swan camp we heard comments that the budget was 'necessary and responsible', while the opposition shadow treasurer described the same outcomes as 'casino economics'. What is economic fact and what is economic fiction...?

Key Forecasts

	08-09	09-10	10-11
Real GDP	0.0	-0.5	2.25
Unemployment	6.00	8.25	8.50
Avg Earnings	4.25	3.25	3.25
CPI	1.75	1.75	1.5
CAD [% of GDP]	5.00	5.25	5.75

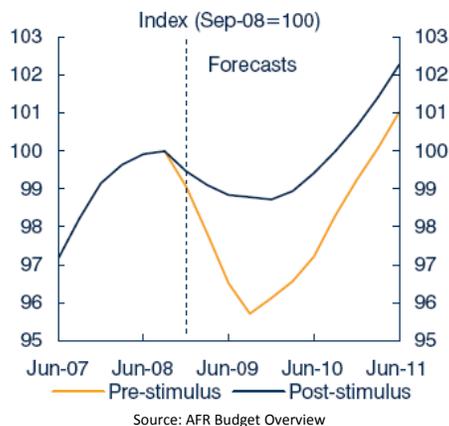
% change on previous year

Source: Budget Papers

Economic Growth

The economy is forecast to contract 0.5% next year followed by a modest 2.25% recovery the following year with above trend growth after that [forecasted to be 4.5% annualised growth]. Business investment is expected to fall by 18.5% in 2009-10 before a weak recovery in the following year and unemployment is forecasted to peak at 8.5% in 2011. Represented by the 'current account deficit' [CAD], net debt is forecast to peak at 13.8 per cent of GDP in 2013-14 before falling again. The budget is also expected to return to surplus by 2015-16.

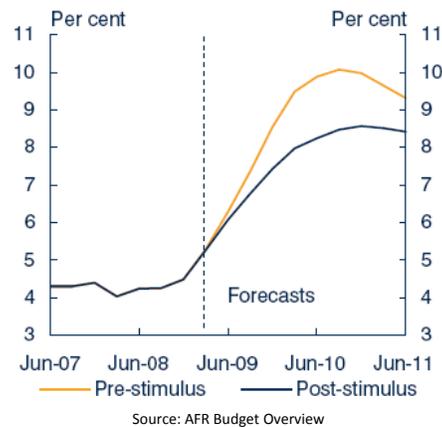
Stimulus effect on real GDP [Graph I]



Business

The centrepiece of the Budget is a significant program of investment in 'nation building' infrastructure, including roads, rail, ports, universities and energy efficiency. The net measures of the Budget are expected to raise the level of GDP by 0.75% in 2009-10 through support in the housing sector, jobs and small businesses.

Stimulus effect on unemployment [Graph II]



- Unemployment to peak at 8.5% in 2011
- Economic growth to contract by 0.5% in 2009-10
- Net debt to peak at 13.8% of GDP in 2013-14

Housing

With housing markets across the world experiencing sharp contractions, Australia has to date remained relatively unscathed. This has been partly supported by fiscal initiatives including the increase in the first home owners grant. With the increase in this grant originally planned to end at 30 June 2009, the Budget includes provisions for this to be extended to 31 December 2009 albeit with a step down in three months.

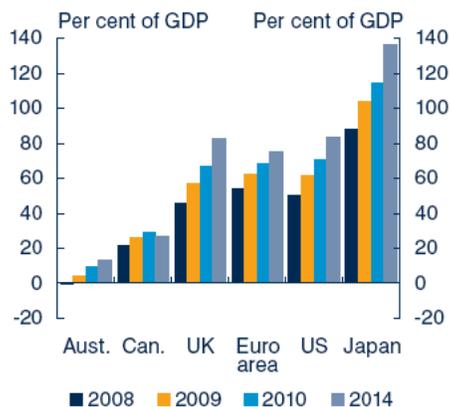
First Home Owners Grant [\$]

	1Jul09 to 30Sep09	1Oct09 to 31Dec09	From 1Jan10
New	21,000	14,000	7,000
Existing	14,000	10,500	7,000

Synopsis

In very simple terms, we cannot see the forecasted growth numbers stack up [-0.5% to +4.5% growth in just four years!]. While Australia appears to be financially and economically well positioned on a relative scale compared to its' developed counterparts, global economic conditions are taking their toll on the domestic economy and these inputs cannot be discounted from forward estimates.

Australia and G7 Public Sector Net Debt [Graph III]



Source: AFR Budget Overview

With national revenue forecasted to decrease by \$210bn over the next four years versus forward estimates, Federal Treasurer Wayne

Swan appears to have resorted to Treasury economic outlooks versus previously used IMF and RBA outlooks. In April 2009, the IMF predicted that the Australian economy would contract by 1.4% versus a forecast of a 0% contraction by Mr Swan. No prizes for guessing which one 'the Treasurer' has used in his latest Budget outlook.

While net debt is expected to peak at 13.8% in 2013-14, this is relatively modest compared with net debt of 80 per cent of GDP for advanced economies in 2014. With reference to Graph I, it "appears" the Treasury may in fact be doing its job in helping cushion what was a necessary contraction.

Two questions that do linger however...

If economic conditions aren't going to be as bad as the 1990's, why is the budget in a worse position? And, if we are entering so called 'unchartered waters', how can the Treasurer be so confident of his economic forecasts over such a short-term period?

Our discussion came to only two conclusions:

1. We can safely expect to see four or five tough and tougher budgets in the periods ahead; and
2. We cannot rely on budget forecasts in an environment dictated by global economic conditions, outside the reach of our domestic Government.

Jai Parrab

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