2004-05 BUDGET PAPER No. 1

BUDGET STRATEGY AND OUTLOOK 2004-05

CIRCULATED BY
THE HONOURABLE PETER COSTELLO MP
TREASURER OF THE COMMONWEALTH OF AUSTRALIA AND
SENATOR THE HONOURABLE NICK MINCHIN
MINISTER FOR FINANCE AND ADMINISTRATION
FOR THE INFORMATION OF HONOURABLE MEMBERS
ON THE OCCASION OF THE BUDGET 2004-05
11 MAY 2004

ISBN 1 74149 132 0

Internet

The Commonwealth budget papers and budget related information are available on the central Budget website at: www.budget.gov.au

Printed by Canprint Communications Pty Ltd

Notes

(a) The following definitions are used in this Budget Paper:

- 'real' means adjusted for the effect of inflation;
- real growth in expenses is measured by the non-farm Gross Domestic Product deflator;
- Budget year refers to 2004-05, while the forward years refer to 2005-06, 2006-07 and 2007-08; and
- one billion is equal to one thousand million.

(b) Figures in tables and generally in the text have been rounded. Discrepancies in tables between totals and sums of components are due to rounding:

- estimates under $100,000 are rounded to the nearest thousand;
- estimates $100,000 and over are generally rounded to the nearest tenth of a million;
- estimates midway between rounding points are rounded up; and
- the percentage changes in statistical tables are calculated using unrounded data.

(c) For the budget balance, a negative sign indicates a deficit while no sign indicates a surplus.

(d) The following notations are used:

NEC/nec	not elsewhere classified
AEST	Australian Eastern Standard Time
-	nil
na	not available
nfp	not for publication
(e)	estimates
(p)	projections
$m	$ million

(e) The Australian Capital Territory and the Northern Territory are referred to as 'the Territories'. References to the 'States' or 'each State' include the Territories. The following abbreviations are used for the names of the States, where appropriate:

NSW	New South Wales
VIC/Vic	Victoria
QLD/Qld	Queensland
WA	Western Australia
SA	South Australia
TAS/Tas	Tasmania
ACT	Australian Capital Territory
NT	Northern Territory

(f) In this paper the term Commonwealth refers to the Commonwealth of Australia. The term is used when referring to the legal entity of the Commonwealth of Australia.

The term Australian Government is used when referring to the Government and the decisions and activities made by the Government on behalf of the Commonwealth of Australia.

Budget Strategy and Outlook 2004-05 is one of a series of Budget Papers that provides information to supplement the Budget Speech. A full list of the series is printed on the inside cover of this paper.

CONTENTS

PART 1: FISCAL STRATEGY AND BUDGET PRIORITIES

PART 2: FISCAL AND ECONOMIC OUTLOOK

PART 3: REVENUE, EXPENSES AND BUDGET FUNDING

PART 4: FINANCIAL REPORTING STANDARDS AND FINANCIAL STATEMENTS

PART 5: PUBLIC SECTOR TRENDS

PART 6: HISTORICAL AUSTRALIAN GOVERNMENT DATA

PART 1
FISCAL STRATEGY AND BUDGET PRIORITIES

This part provides an overview of the fiscal and economic outlook, describes what the government is achieving with its fiscal strategy and outlines the key budget priorities.

STATEMENT 1: FISCAL STRATEGY AND BUDGET PRIORITIES

The Government's fiscal strategy puts Australia at the forefront of the developed world. The 2004-05 Budget puts in place a series of major initiatives aimed at boosting Australia's economic growth potential, and addressing the ageing of the population through increased participation and productivity.

In this Budget the Government introduces large increases in assistance to families, improves incentives for women to re-enter the workforce after having children, continues its commitment to structural tax reform and by increasing the co-contribution to superannuation, provides significant incentives to save for retirement.

The Government's *More help for families* package will provide substantial assistance and improved rewards from work for families through changes to the Family Tax Benefit (FTB), along with a one-off lump sum payment to all families who are eligible for, or receive FTB (A) in 2003-04.

The Government will also improve the rewards from work by lifting tax thresholds so that more than 80 per cent of Australians will be in the 30 per cent tax bracket or lower, with effect from 1 July 2004.

The Budget enhances the co-contribution to superannuation, boosting incentives for low and middle income earners to make additional superannuation contributions. Further cuts to the superannuation surcharge will also boost retirement savings.

The Government is also seeking to improve productivity through a $5.3 billion boost to science and innovation, as well as $3.1 billion funding for AusLink, the new land transport infrastructure programme.

With the improvement of international economic conditions with growth in the United States, Japan and South-east Asia, the Australian economy is forecast to continue to grow strongly at 3 ½ per cent with unemployment forecast to remain at 23 year lows of 5 ¾ per cent.

Having met the need for further family assistance, tax cuts, and for spending in priority areas, the Budget is still forecast to be in surplus with an underlying cash balance of $2.4 billion in 2004-05.

CONTENTS

STATEMENT 1: FISCAL STRATEGY AND BUDGET PRIORITIES

FISCAL OUTLOOK

The fiscal outlook for Australia remains positive, with the forecast of a seventh Budget surplus. Australia is in a much stronger fiscal position than most comparable economies. Across the forward estimates, the Government has maintained the budget in surplus, after providing for its *More help for families* package, consisting of $19.2 billion for assistance to families, $14.7 billion for structural tax reform and $2.7 billion to boost retirement savings.

The 2004-05 Budget puts in place a series of major initiatives, particularly enhanced family assistance and further tax reforms, aimed at boosting Australia's medium-term growth potential and addressing the ageing of the population through increased participation and productivity.

An underlying cash surplus of $2.4 billion is expected in 2004-05 compared with an estimated surplus of $3.8 billion at the *Mid-Year Economic and Fiscal Outlook 2003-04* (MYEFO). Underlying cash surpluses continue to be projected across the forward estimates.

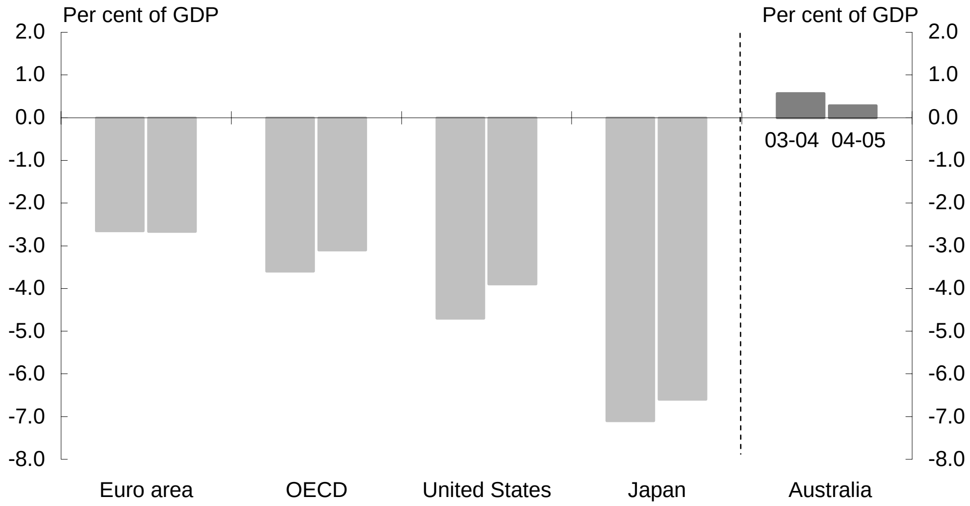
Table 1: Budget aggregates

	Actual	Estimates		Projections		
	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Underlying cash balance ($b)	**7.5**	**4.6**	**2.4**	**1.6**	**3.4**	**4.5**
Per cent of GDP	1.0	0.6	0.3	0.2	0.4	0.4
Fiscal balance ($b)	**6.0**	**3.0**	**0.7**	**0.7**	**2.3**	**2.6**
Per cent of GDP	0.8	0.4	0.1	0.1	0.2	0.3

In accrual terms, a fiscal surplus of $0.7 billion is now expected for 2004-05 compared to a surplus of $1.6 billion estimated at MYEFO.

Australia's very strong fiscal position compared to most comparable developed economies is highlighted in Chart 1. The latest OECD projections show that most of the major advanced economies are expected to record deficits in 2004 and 2005. The United States is expected to record a deficit of 4.9 per cent of Gross Domestic Product (GDP) in 2005, with significant deficits also expected in Japan and the European area.

Chart 1: International comparison of budget balances 2004 and 2005



Source: OECD Economic Outlook 74 December 2003 and Budget Paper No. 1, *Budget Strategy and Outlook 2004-05*.

ECONOMIC OUTLOOK

The outlook for the Australian economy is for continued growth, with increasing employment and low inflation. A stronger world economy in 2004-05 will support a rebalancing of growth from domestic to external sources. In year-average terms, GDP growth is forecast to moderate slightly from 3¾ per cent in 2003-04 to 3½ per cent in 2004-05. The recovery in farm production will continue, assuming average seasonal conditions.

Unemployment is forecast to remain near 23 year lows during 2004-05, supported by moderate wage outcomes. The combination of strong growth, low inflation and low unemployment represents a sound basis for future growth and is a major achievement for the Australian economy.

Table 2: Major economic parameters (percentage change from previous year)

	Forecasts		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
Real GDP	3 3/4	3 1/2	3 1/2	3 1/2	3 1/2
Employment(a)	1 3/4	1 3/4	1 1/2	1 1/2	1 1/2
Wages(b)	3 3/4	3 3/4	3 3/4	3 3/4	3 3/4
CPI	2 1/4	2	2 1/2	2 1/2	2 1/2

(a) Labour force survey basis.
(b) Wage Cost Index.
Source: Australian Bureau of Statistics (ABS) Cat. No. 5206.0, 6202.0, 6401.0, 6345.0 and Treasury.

FISCAL STRATEGY

The Government's medium-term fiscal strategy is an integral part of a macroeconomic framework through which the economy can deliver sustainable economic growth, rising employment and higher living standards.

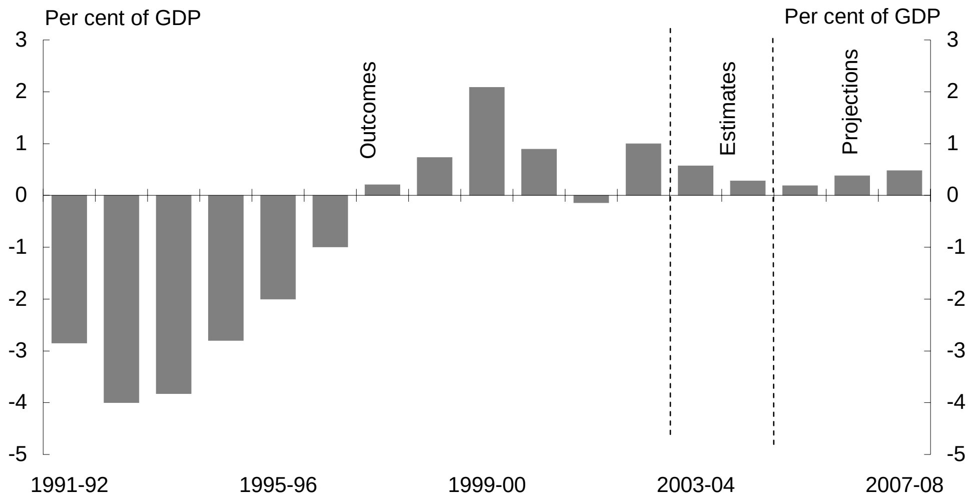
A medium-term approach to fiscal policy

The primary objective of the Government's medium-term fiscal strategy is to maintain budget balance, on average, over the course of the economic cycle. This ensures that the Government is not living beyond its means. It helps deliver macroeconomic stability, encourages private investment in a low interest rate environment, entrenches low public debt and ensures that, over time, the current account reflects private saving and investment decisions.

The Government's medium-term fiscal strategy has a number of supplementary objectives, including maintaining budget surpluses over the forward estimates period while growth prospects are sound, not increasing the overall tax burden from 1996-97 levels and improving the Australian Government's net worth position over the medium to longer-term. The supplementary objective of no increase in the overall tax burden means that the Government achieves balance over the cycle through a disciplined and prioritised approach to spending and not by recourse to increased taxation.

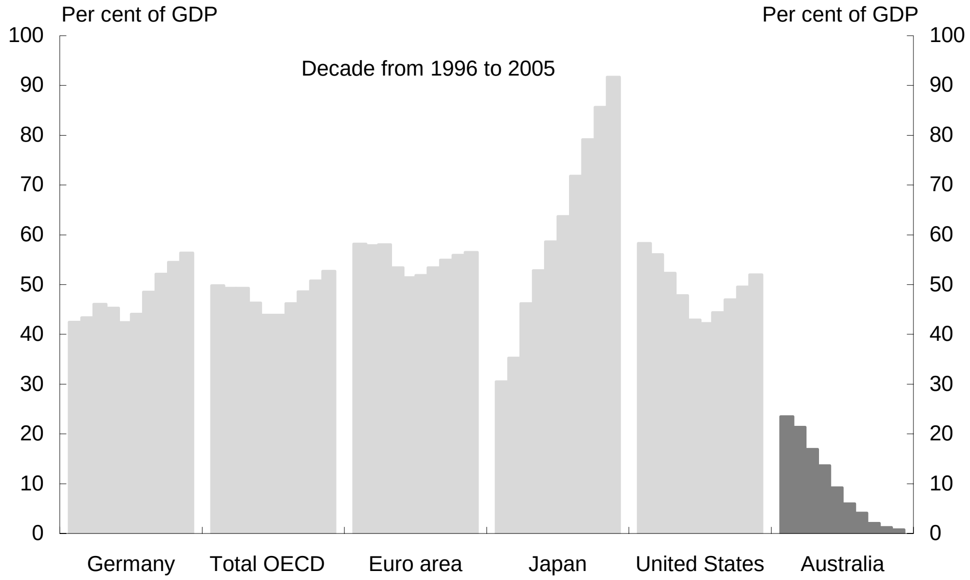
Over the seven years to 2003-04 the Australian Government's cumulative underlying cash surpluses have amounted to around $35.7 billion (Chart 2).

Chart 2: Underlying cash balances



The long-term fiscal pressures facing the Australian Government place a premium on maintaining good fiscal policy in the years ahead. The Government has a strong record on fiscal policy and in particular fiscal sustainability, having already delivered a major reduction in the level of general government net debt. Australia now has one of the lowest levels of net debt in the OECD (Chart 3).

Chart 3: General government net debt levels in selected countries[a]



(a) International data are sourced from OECD Economic Outlook 74 December 2003. Australian data are sourced from Statement 12, Table A4. All data are for the total general government sector.

The Government's supplementary objective of improving net worth over time from the significantly negative position inherited from the early 1990s, contributes to fairness and equity between generations. The improvements in net debt and net worth have been made possible by adherence to the primary objective of balancing the budget over the cycle.

Full details of the medium-term fiscal strategy are set out in Appendix A to this statement.

BUDGET STRATEGY AND PRIORITIES

The release by the Government of the Budget Paper No. 5, *Intergenerational Report 2002-03* with the 2002-03 Budget highlighted that, due to the projected doubling in the proportion of the population aged 65 or more and other factors, there will be significant increases in government spending on areas such as health, aged care and age pensions over the next 40 years. At the same time, it projected that growth in the proportion of the population of workforce age will slow to almost zero over that period.

As a result, the Intergenerational Report projected that there would be a gap between the level of Government spending and the revenue raised through taxes of around five per cent of GDP by 2042.

Such a gap can be addressed in a number of ways:

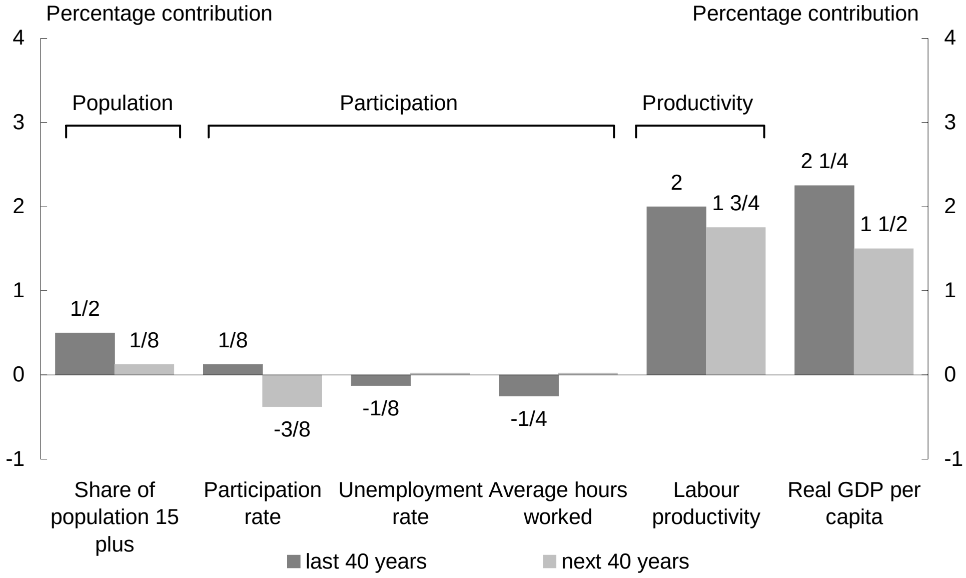
- One way is to increase taxes. A second is to run large deficits and leave the resulting debt burden to future generations. The Government does not support either of these alternatives.

- A third alternative is to cut government expenditure. The Government is taking steps to ensure that spending in areas such as health and social security is maintained at sustainable levels into the future. However, announced measures such as increasing co-payments under the Pharmaceutical Benefits Scheme and moderating the growth in spending on the Disability Support Pension are yet to be passed by the Senate. Whilst expenditure restraint is an integral part of meeting the demographic challenge, the scope for reducing expenditures is not sufficient to meet the demographic challenge.

- A fourth, preferred approach is to grow the economy faster so that Australia generates sufficient income to enable it to continue to improve living standards and meet the increased costs associated with an ageing population, without increasing taxes as a proportion of GDP or leaving higher debt burdens for future generations.

Chart 4 shows the contributions that population growth, labour force participation and productivity in the economy have made to real average annual growth in GDP per person in Australia over the past 40 years and the projections for the next 40 years. Those projections indicate that, in the absence of policy changes, it is likely that real GDP per person will slow to around 1½ per cent per annum over the next 40 years, relative to around 2¼ per cent per year over the past 40 years. This is due largely to the negative contribution to growth of the projected decline in labour force participation — a direct result of the ageing of the population — and a return to the long term growth rate of productivity of 1¾ per cent a year.

Chart 4: Contributions to GDP per capita growth



These issues have been explored in depth in the Discussion Paper *Australia's Demographic Challenges* released by the Treasurer in February 2004. That paper highlights the need to take early action to increase productivity and labour force participation. It notes that the sooner steps are taken to address these issues, the more successful Australia will be in boosting its medium-term growth potential and addressing the ageing of the population that is already underway.

Boosting GDP per capita growth is valuable for other reasons, but it will also help to address the fiscal challenge highlighted by the Intergenerational Report. Other things being equal, participation and productivity measures that contributed an additional half of a percentage point to average annual GDP per capita growth would prevent government spending from increasing as a proportion of GDP as the population ages.

The 2004-05 Budget puts in place a package of major initiatives that address directly these key objectives of increasing participation and productivity. Together, they represent a further significant step in the Government's programme of economic and social policy reform that, over time, will ensure that Australia is able to continue to lift its standard of living, while also dealing effectively and sustainably with the ageing of its population.

The major initiatives in this Budget are consistent with these longer-term objectives. They assist with the cost of raising children, reduce welfare traps for those receiving family tax benefits and deliver tax cuts to increase the rewards from working.

Participation

Australia's Demographic Challenges set down three key areas where action is needed to improve labour force participation:

- improving incentives to work and save for retirement;
- improving the capacity of people to undertake work; and
- supporting more flexible work options.

Work and savings incentives

The centrepiece of the 2004-05 Budget is the Government's *More help for families* package that continues the Government's commitment to assist Australian families, ongoing structural tax reforms and incentives to save for retirement. The total package amounts to $37 billion over five years. There are three elements:

- increased assistance to Australian families and reductions in effective marginal tax rates for families;
- income tax cuts to reduce the disincentive of high marginal tax rates; and
- incentives to save for retirement through an enhanced superannuation co-contributions scheme and a reduction in the superannuation surcharge.

The package builds on the substantial reforms put in place under *The New Tax System*.

More help for families

The 2004-05 Budget includes the largest package of assistance for families ever, with an additional $19.2 billion being provided over five years. The package builds on, and expands, the large increases in assistance for families introduced in *The New Tax System* in 2000 and the Family Tax Initiative announced in 1996.

The package increases the adequacy of assistance for all families with dependent children and improves rewards from work for low and middle income families in particular.

It includes the following elements:

- An increase in the rate of Family Tax Benefit (FTB) (A) of $600 per child to be paid as a lump sum upon reconciliation of entitlement following the end of the financial year, commencing in respect of the 2003-04 financial year. The annual lump sum will be available, if required, to offset any overpayment of FTB that may have occurred during a previous year. FTB (A) is currently payable to families with incomes up to $85,702 for one child, $92,637 for two children and $99,572 for three children.

- In order to provide an immediate benefit a lump sum payment of $600 per child will be paid before 30 June 2004 to all families receiving or eligible for FTB (A) in the 2003-04 financial year. This means eligible families will receive $600 per child before 30 June 2004 and be entitled to a further $600 per child after the reconciliation of their 2003-04 entitlement. As a consequence most families will be eligible for an additional $1,200 per child in the next 12 months.

- A reduction in the income test taper rate for the maximum rate of FTB (A) from 30 per cent to 20 per cent, with effect from 1 July 2004. This builds on the taper reduction from 50 per cent to 30 per cent undertaken in *The New Tax System*. This will improve rewards from working for low and middle income families. In particular it means that for each additional dollar of income, eligible families lose only 20 cents rather than 30 cents of family payment. Combined with the $600 per child per annum rate increase, it will provide substantial additional assistance to families with incomes up to $87,702 for one child and higher levels for subsequent children.

- A relaxation of the income test for FTB (B), with the income test threshold for the secondary earner in a family being increased from the current level of $1,825 a year to $4,000 a year and the income test taper being reduced from 30 per cent to 20 per cent:

  – this too builds on the income test relaxations in *The New Tax System*, which also increased the rate of FTB (B). The current maximum rate is $2,920 per year for a family with a child under five and $2036.70 for families with a child aged between five and 16;

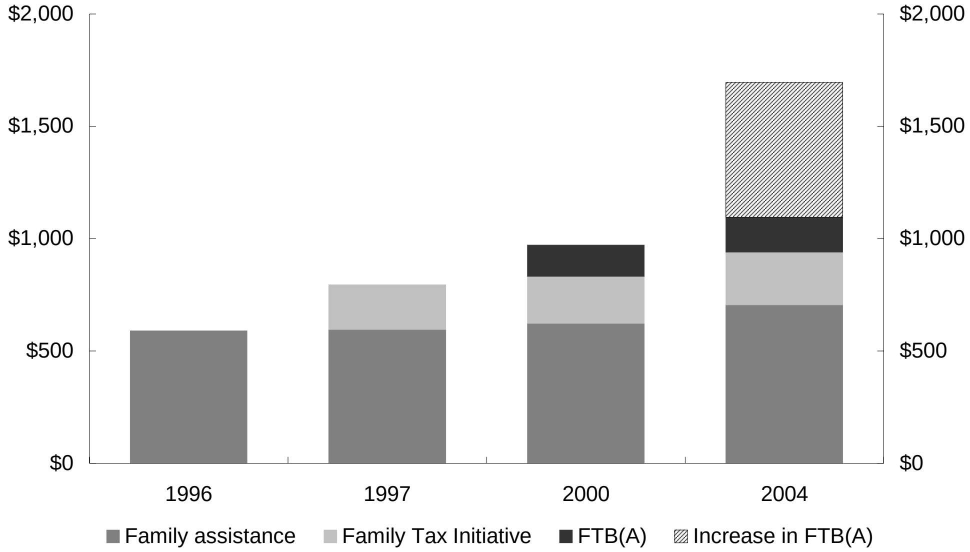
  – it will improve incentives for a second earner in a family to take up part time or casual work, providing additional assistance for those combining work and family responsibilities.

- Mothers returning to work will also be assisted by the quarantining of FTB (B) payments. This means that income they receive from returning to work will not count against their eligibility for FTB (B) already received in that year prior to commencing work.

- The introduction from 1 July 2004 of a new Maternity Payment, paid as a lump sum, of $3,000 for each new born child. This will be a universal payment to all families (usually the mother). This payment will increase to $4,000 from 1 July 2006 and increase again to $5,000 from 1 July 2008. This new payment will incorporate the existing Maternity Allowance and the Baby Bonus, with the Baby Bonus still available for births prior to 1 July 2004.

Chart 5 below shows the total increase in the base rate of assistance for families through FTB (A) and its predecessors since 1996. Over this period the Government has increased the maximum and base rates of payments by $940 per child per year — a real increase in the base rate of over 100 per cent.

Chart 5: Increases in base rate per child assistance to families since 1996



Income tax cuts

Building on the substantial income tax cuts provided in *The New Tax System* and in the 2003-04 Budget, the Government will introduce new thresholds for marginal tax rates which will cut income tax by $14.7 billion over four years. This will ensure that high marginal tax rates are not a disincentive for those taking on additional work, wishing to work overtime, seeking promotion or improving their skills or productivity. The thresholds will be lifted in two stages:

- from 1 July 2004 the 42 per cent threshold will be increased from $52,001 to $58,001 and the 47 per cent threshold will be increased from $62,501 to $70,001;
- from 1 July 2005 the 42 per cent threshold will be further increased to $63,001 and the 47 per cent threshold to $80,001.

Table 3: New personal tax rates

Current tax thresholds Income Range ($)	New tax thresholds from 1 July 2004 Income Range ($)	New tax thresholds from 1 July 2005 Income Range ($)	Tax rate
0 - 6,000	0 – 6,000	0 – 6,000	0
6,001 - 21,600	6,001 – 21,600	6,001 – 21,600	17
21,601 - 52,000	21,601 – 58,000	21,601 – 63,000	30
52,001 – 62,500	58,001 – 70,000	63,001 – 80,000	42
62, 501 +	70,001 +	80,001 +	47

Improved rewards from participating in the workforce will flow from taxpayers being able to earn more without moving into a higher tax bracket and from moving taxpayers onto lower marginal tax rates.

- The income range over which the 30 per cent marginal tax rate will apply will be significantly increased with the result that more than 80 per cent of taxpayers will be in the 30 per cent tax bracket or lower over the forward estimates period.

- Taxpayers on average full-time weekly earnings will remain in the 30 per cent tax bracket over the forward estimates period, even allowing for ongoing wages growth.

- The increase in the top threshold will make Australia's personal tax system more internationally competitive, providing incentives for skilled Australians to stay and work in Australia.

The combined effect of the three stages of tax reform has been to deliver significant tax cuts for all Australians.

- Taxpayers earning $20,000 paid $2,770 in income tax prior to *The New Tax System* (excluding the Medicare levy) whereas taxpayers on that income would now only pay $2,145, a reduction of around 23 per cent in tax.

- Taxpayers on $50,000 (around average weekly earnings) paid $14,102 in income tax prior to *The New Tax System* (excluding the Medicare levy), compared with $11,172 now, a reduction of around 21 per cent.

- By 1 July 2005, a taxpayer on $90,000 who paid $32,902 in tax prior to *The New Tax System* (excluding the Medicare levy) will pay $26,912 in tax in 2005-06, a reduction of around 18 per cent.

In an increasingly globalised world economy with increased mobility of both capital and labour, it is critical that Australia maintains an environment that is competitive with other developed nations. The income tax cuts outlined in this Budget will help ensure that Australia is able to retain people with highly regarded skills. This complements the measures the Government has implemented and proposed arising from the *Review of International Taxation Arrangements*.

Overall, these changes to family assistance, and the tax scales will significantly assist families with the costs of raising children. They will also improve rewards from work for Australian taxpayers and families by reducing tax and easing the withdrawal of family assistance.

Incentives to save for retirement

The Government's retirement income policy provides incentives to make additional voluntary savings through the superannuation system for those who want more retirement income than the current compulsory superannuation and social security arrangements will provide.

The Government will provide $2.1 billion over the next four years to enhance the superannuation co-contribution scheme. This will significantly boost incentives for low and middle income employees on incomes up to $58,000 per year to make additional personal superannuation contributions.

In this Budget, the Government co-contribution will be increased to 150 percent of an employee's contribution up to a maximum of $1,500. The income threshold, up to which the maximum co-contribution applies, will increase to $28,000 (from $27,500) and extend the maximum benefit to a significantly wider number of employees. The maximum co-contribution will reduce by 5 cents for each dollar of income to phase out completely at $58,000. Currently the co-contribution phases out completely at $40,000. People on incomes between $40,000 and $58,000 will become eligible for a co-contribution for the first time.

These enhancements build on the extension of the co-contribution arrangements announced by the Government on 14 March 2004 to cover more low income earners at a cost of $195 million over the forward estimates period.

The Government will also further reduce the maximum superannuation surcharge rates to increase the incentive for higher income individuals to make contributions, at a cost of $610 million over the next four years. The rate will progressively reduce from its original level of 15 per cent to 7.5 per cent in 2006-07. Low and middle income earners will receive more than three quarters of the benefits of these superannuation changes.

The Government is also seeking to make the retirement income system more flexible by broadening the availability of superannuation, providing more choices in financing retirement income, making superannuation more adaptable to changing work arrangements and improving the integrity of the system. These changes were announced on 25 February 2004 in the statement, *A more flexible and adaptable retirement income system*.

The capacity to work

As noted in *Australia's Demographic Challenges*, equipping people with adequate skills is an important determinant of their capacity to participate in the labour force. Equally, ensuring that people remain healthy increases their capacity to participate.

The Government has announced a series of major initiatives over the past year that will contribute to improving educational outcomes and, over time, the level of skills in society. These include the higher education reforms announced in the 2003-04 Budget, the new vocational education arrangements with the States (also announced in the 2003-04 Budget) and most recently, the new funding arrangements for schools. Over the next four years, the Government will increase funding for schools by over $8 billion to $32 billion in total. This will provide additional funding for both government and non-government schools.

In this Budget, the Government has also allocated funding for its expanded commitment to improving early childhood development through early intervention programmes that help young children grow up in stable and supportive environments. These programmes focus on children in need and aim to improve their life chances so that they can have a substantive and productive involvement in society as they grow up.

Since coming to office, the Government will have doubled funding for health and aged care by 2004-05. The Government's $2.85 billion MedicarePlus package ensures that Australians have continued access to affordable primary health care. Along with the Government's $42 billion contribution to the cost of hospital care and the funding of the Pharmaceutical Benefits Scheme, it ensures that high quality, affordable health care is available quickly for those who need it. This is supported by substantial investment in preventative health measures. Together, these programmes ensure that Australians are able to remain healthy and participate in the workforce and the community.

More flexible work options — balancing work and family

Since 1996, the Government has put in place a wide range of measures that are aimed at enhancing workplace flexibility. The *Workplace Relations Act 1996* has simplified labour relations and allowed employers and employees to tailor wages and conditions to the specific skills and needs of particular individuals and jobs. However, further flexibility is needed. Accordingly, the Government has sought for some time to reform unfair dismissal laws, improve bargaining processes and other improvements. These remain before the Senate.

The availability of flexible work options, such as part time and casual work, can make a substantive contribution to increasing overall participation in the labour force. Many people, particularly women combining work and family responsibilities, prefer such flexible arrangements. It is important that the labour market accommodates such choices and that supportive policies, such as child care, are available to people wanting to exercise such choices.

In this Budget, the Government demonstrates its ongoing commitment to assisting families balancing work and family commitments. The new Maternity Payment will assist families at the birth of each child. In addition, the Government will increase significantly its commitment to supporting the provision of quality and affordable child care. Additional measures include an expansion of the number of outside-school-hours care places by 40,000 and an expansion of family day care places by 4,000. These additional places will help support working families, particularly women wishing to re-enter the labour force after having children.

Investing in Australia's health

The Government's ongoing policy reform process is focused on long term economic and social objectives of enhancing the living standards of all Australians and dealing with our ageing population. This Budget furthers that process by boosting support for carers, improving access and quality of aged care and meeting our obligations to our veterans.

Investing in Australia's aged care: more places, better care

Following the Review of Pricing Arrangements in Residential Aged Care, the Government is providing $2.2 billion over five years to ensure that the aged care sector is able to continue to provide affordable and quality aged care for the increasing number of older Australians requiring aged care services ensuring fair and equitable access. Importantly, it will enhance the efficiency and viability of the sector, improving the capacity of providers to generate sufficient income to enable them to finance the ongoing expansion of the supply of places required as the population ages.

Major elements of the package are:

- increased subsidies to providers for the care of residents through the introduction of a Conditional Adjustment Payment. This will deliver an extra $878 million in recurrent resources;
- an additional $101 million for improving the aged care workforce through funding for training specialised aged care nurses and the upgrading of skills;
- additional funding of $58 million in 2006-07 and 2007-08 to enable the Government to meet its 2001 election commitment of 108 aged care places for every 1000 Australians aged 70 years or more; and
- an increase in accommodation charges for new high-care residents by up to $2.34 per day to $16.25 per day to improve providers' ability to finance expanded and improved facilities, with a corresponding increase in subsidies for financially

disadvantaged residents. This will deliver an additional $439 million in capital funding.

The Government will also provide $513 million in 2003-04 to finance improved safety and building standards for aged care homes, developed and agreed with the industry. A one-off $3,500 payment will be made to providers for each resident in an aged care facility before 30 June this year.

Recognising the contribution of carers

Carers provide a great service to the community through supporting and caring for those with disabilities. The Government values this contribution and is providing an additional $461 million to carers over five years from 2003-04 to 2007-08 with the following components:

- $255 million for a one-off carer bonus to be paid in June 2004. Recipients of Carer Payment will receive a $1,000 payment, and recipients of Carer Allowance will receive a $600 payment, in recognition of their contribution in their role of carer to someone with a disability;
  - Carer Payment is paid to a person with limited other income who provides constant care for someone with a disability, while Carer Allowance is an income supplement paid to someone who lives with and provides daily care and attention to a person with a disability;
- $107 million to expand the eligibility criteria for Carer Allowance to enable carers who provide at least 20 hours of personal care per week but do not live with the care recipient to receive the payment; and
- $99 million to expand the access of carers to respite services. Ageing parents caring for adult children will be entitled to up to four weeks respite a year, depending on their circumstances, subject to matched funding from the States. Young carers aged under 25 years will benefit from expanded access to in-home respite care in addition to a range of information, referral and advice services. This will support young carers at risk of leaving education prematurely and not completing secondary or equivalent education.

Additional support for veterans

The Government places a high priority on meeting its obligations to those who have served in the defence of Australia. This Budget provides additional funding to veterans of $443 million. Key measures are:

- a $289 million package over five years to provide extra assistance to veterans and their families in response to the Clarke Review. This includes a new Defence Force Income Support Allowance, payable to certain disability pensioners who also receive income support payments; indexation of the above general rate component of disability pension according to movements in male total average weekly earnings; and payment of rent assistance to war widows in addition to the income support supplement;

- $158 million over four years to ensure that veterans can continue to have access to medical specialists by increasing the fees the Government pays to specialists for seeing veterans; and
- redevelopment of the Australian War Memorial's Post-1945 Galleries and continuation of the existing commemorations programme and the repair and replacement of war graves programme.

Investing in Australia's science and innovation

In this Budget, the Government continues to put in place measures that will contribute to a policy framework that promotes productivity growth. These measures build on the substantive reforms put in place since 1996, including the medium term monetary and fiscal policy framework, personal, company and indirect tax reform, labour market reforms, enhancement of financial sector regulation, reductions in tariff assistance, competition reforms and commercialisation and privatisation of government business enterprises.

Science and innovation plays a crucial role in lifting Australia's future productivity. They significantly enhance economic growth and create new employment opportunities.

A key feature of this Budget is the extension of the Government's Backing Australia's Ability (BAA) package. The successor programme, *Backing Australia's Ability – Building our Future through Science and Innovation*, will provide funding of $5.3 billion over seven years from 2004-05, a sizeable contribution that reaffirms and strengthens the Government's ongoing commitment to science and innovation. Key elements of the package include:

- an ongoing commitment to high quality research through:
  - additional funding for bodies such as the Australian Research Council (additional funding of $1.2 billion over seven years), the National Health and Medical Research Council (an additional $200 million over seven years) and CSIRO (an additional $305 million over seven years will be invested in the National Flagships Initiative);
  - funding of $542 million for the National Collaborative Research Infrastructure Strategy which will link Australian Government investment in research infrastructure to the national research priorities;
- additional funding for the commercialisation of research through:

  - $1 billion for the new Commercial Ready Programme that will provide support to firms to undertake research and development with strong commercialisation potential;
  - an extra $100 million over seven years for the Commercialising Emerging Technologies Programme which provides innovators with advice and financial assistance to plan their commercialisation, attract capital for their project and to establish strategic partnerships to take the innovation to market; and
- initiatives that develop critical skills, including in disciplines such as mathematics and science.

Investment in Australia's infrastructrue — *AusLink*

The provision of quality physical infrastructure is crucial to increasing efficiency and productivity in the economy. In this Budget, the Government will introduce a new land transport infrastructure programme — *AusLink*.

Over the next five years, an additional $1.9 billion will be allocated to upgrade Australia's road and rail systems. This includes $810 million over three years from 2006-07 redirected from the Fuel Sales Grants Scheme announced in January 2004 and a grant of $450 million in 2003-04 to the Australian Rail Track Corporation. This sum will be used to invest in new rail infrastructure projects on the interstate rail system. This additional national network funding will position Australia to cope with an expected doubling of the land freight task over the next 20 years.

In January 2004, the Government also announced the extension, for four years from 2005-06, of the Roads to Recovery programme costing $1.2 billion within the *AusLink* framework.

The *AusLink* White Paper will be released in June 2004.

Investing in Australia's security

A strongly performing economy can only be sustained within a safe and secure environment for our nation and community.

The heightened threat posed by terrorism continues to require the Government to move quickly to upgrade national security arrangements. A strong defence capability, aligned with Australia's strategic interests, also remains a key priority for the Government.

The 2004-05 Budget provides a further $755 million over the five years from 2003-04 to improve intelligence capabilities; incident response; protective security; border security; and security capacity and cooperation in the region. In total, the Government has committed $3.1 billion over seven years since 11 September 2001 to make Australia more safe and secure. This Budget includes:

- $270 million to strengthen Australia's intelligence capabilities including through increased funding for continuing to build the capabilities of the Australian Security Intelligence Organisation (ASIO) ($127 million over four years) and the Australian Secret Intelligence Service (ASIS) ($46 million over four years), and enhancing Defence's intelligence operations and analytical capability ($47 million over four years);

- an additional $207 million to upgrade protective security, including expansion of the Air Security Officer programme to include additional priority international destinations;

- $40 million to build further Australia's capacity to respond to incidents. The national medicines stockpile will be expanded and improvements will be made to the biosecurity surveillance system;

- $150 million to help secure Australia's borders, through more robust identity verification processes utilising biometric technology and an integrated global visa processing system; and

- a further $87 million to improve security capacity and cooperation in the region, including through the Australian Federal Police.

In recent years, the Government has provided substantial new funding for significantly enhanced defence capabilities and levels of preparedness, and provided for the Australian Defence Force's participation in international operations. The 2004-05 Budget continues this approach. Measures in the 2004-05 Budget exceed $1.5 billion over five years, bringing to $39.7 billion the total amount of additional defence spending by the Government since 1996. Key measures include:

- a continued commitment to participation in international operations. The Government will provide $132 million for the Australian Defence Force's contribution to the stabilisation and reconstruction of Iraq. This will allow for continuation of the deployment through financial year 2004-05. The timeframe for, and composition of, Australia's commitment in Iraq will be kept under review. The Government will also provide $20 million for an expected extension of Defence's contribution to the United Nations mission in East Timor;

- a further $205 million funding for logistics support, including for the F/A-18 fighter aircraft fleet and Collins class submarines, along with an additional $610 million over four years for other high priority platforms including the refit of the HMAS *Success* and support for PC-9 aircraft and army and naval aviation; and

- $458 million over the next four years for a range of personnel initiatives, including $357 million to increase the quality of, and access to, housing for members of the Australian Defence Force without dependents and for rental assistance for those without dependents.

Our land, environment and people

A continuing high priority for the Government is to support economic and social development in rural and regional Australia, to ensure economic development is environmentally sustainable, and that our migration and resettlement programme delivers benefits, including to regional Australia.

Assisting rural and regional Australia

The drought that has affected around 62 per cent of Australia's productive agricultural land over the last two years has had major economic and social impacts. In some areas recovery is underway, while in others drought conditions persist.

The Government will provide $73 million over three years to primary producers in regions that have been declared eligible for Exceptional Circumstances assistance since December 2003. This assistance includes income support and interest rate subsidies. Over all, the Government expects to provide $1.1 billion in direct drought assistance to farmers and their communities over the period 2002-03 to 2005-06.

This Budget also includes a $444 million package for the sugar industry aimed at helping the industry through the transition to restructure, diversify and provide long term certainty for the industry and the regional communities that depend on it.

Further support will be provided to primary producers through the Agriculture-Advancing Australia package, which will receive funding of $236 million over four years. Programmes under the Agriculture-Advancing Australia package, including FarmBis, FarmHelp and the Regional Financial Counselling Service, aim to equip primary producers with the skills and support necessary to respond positively to change, to adopt and benefit from innovation and to meet the challenges of farming in Australia.

The Government will rebate $290,000 of wine equalisation tax (WET) to every wine producer per annum. This measure will apply from 1 October 2004 and will be pro-rated for the 2004-05 financial year. The effect of this decision is to exempt $1 million dollars of each producer's domestic wholesale wine sales from the WET on an annual basis. Around 85 per cent of the benefit of this change will be received by small wine producers in rural and regional Australia.

Further improvements to the affordability and access to vital health services in rural and regional Australia remains a strong Government commitment. Accordingly, funding for the Rural Health Strategy is being renewed at a cost of $830 million over four years to address gaps in and access to health services in rural and remote areas and to increase the rural health workforce.

The Government is further strengthening its commitment to the development of self-reliant regional communities by providing $78 million over four years to the Regional Partnerships programme.

Sustaining our environment

The Government is committed to curbing Australia's greenhouse gas emissions in a manner that maintains Australia's strong and internationally competitive economy.

Funding of $248 million will be provided over the period 2004-05 to 2007-08 to implement the Government's Climate Change Strategy. The Climate Change Strategy will encourage industry and the community to reduce emissions, and facilitate Australian industry's preparedness to respond to the future challenges posed by climate change. Funding of $27 million will foster the development of innovative low emissions technologies, with $31 million for scientific research to better understand and predict how future changes in Australia's climate will affect our environment, communities and industry.

The World Heritage listed Great Barrier Reef is a significant part of Australia's unique natural environment, supporting coastal communities and a vibrant tourism industry. From 1 July 2004, the size of 'no take' fishing areas will increase from less than 5 per cent to 33 per cent of the Great Barrier Reef Marine Park. To support this, the Budget provides $23 million for activities such as enforcement, compliance and education associated with the implementation of this change.

Migration and resettlement

Australia's strong commitment to a large, ongoing migration programme has delivered significant economic and social benefits. In 2004-05, the programme will increase by up to 6,000 places to a maximum of 120,000 places, with an additional 1,000 places for medical practitioners and their families and 5,000 places for skilled migrants living and working in regional Australia. The Australian Government has also increased the size of the Refugee Programme, from 4,000 to 6,000, within an increased total Humanitarian Program of 13,000.

Orderly resettlement of humanitarian entrants and migrants is crucial to the success of Australia's migration and humanitarian programmes. The Government is providing additional funding of $268 million over four years to enhance key settlement and other services for an increased number of humanitarian entrants and migrants, including those settling in regional Australia.

Support for the Commonwealth Games

Reflecting Australia's proud sporting heritage and recognising the opportunity to secure longer term benefits from showcasing Australia to the world, the Government will provide assistance for the staging of the 18th Commonwealth Games (M2006) in Melbourne in 2006.

The Government will provide $273 million over four years from 2003-04, including $140 million in new funding with a further $133 million in services and support which will be absorbed from within existing resources. Key elements include:

- a $103 million grant to the Victorian Government to meet the cost of specific M2006 initiatives, such as the Opening and Closing Ceremonies;
- $85 million to enhance security arrangements in the lead-up to and during the Games; and
- an estimated $55 million for the Australian Sports Commission to assist Australian athletes to perform at their best.

APPENDIX A: MEDIUM-TERM FISCAL STRATEGY

The Government's medium-term fiscal strategy is an integral part of the macroeconomic framework that creates an environment in which the economy can deliver sustainable economic growth, rising employment and higher living standards.

A medium-term approach to fiscal policy

The primary objective of the Government's medium-term fiscal strategy is to maintain budget balance, on average, over the course of the economic cycle.

The supplementary objectives of the fiscal strategy are:

- maintaining budget surpluses over the forward estimates period while economic growth prospects remain sound;
- no increase in the overall tax burden from 1996-97 levels; and
- improving the Australian Government's net worth position over the medium to longer term.

The primary fiscal objective of budget balance over the cycle ensures that the Government is not living beyond its means. It helps deliver macroeconomic stability, encourages private investment in a low interest rate environment, entrenches low public debt and ensures that, over time, the current account reflects private saving and investment decisions. The supplementary objective of no increase in the overall tax burden means that the Government achieves balance over the cycle through a disciplined and prioritised approach to spending and not by recourse to increased taxation. Consequently, an important element in achieving the strategy is containing spending growth by eliminating waste and placing programme spending on a sustainable basis.

A credible and sustainable framework

The broader budgetary framework of discipline, transparency and accountability underpinning the Government's fiscal strategy is embodied in the *Charter of Budget Honesty Act 1998* (the Charter). The purpose of the Charter is to improve fiscal policy outcomes. It achieves this by requiring that fiscal strategy be based on principles of sound fiscal management (Box 1) and by facilitating public scrutiny of policy settings and performance.

Box 1: *Charter of Budget Honesty Act 1998* — Principles of sound fiscal management

The Charter states that fiscal policy should be directed at maintaining the economic prosperity and welfare of the people of Australia and therefore should be set in a sustainable medium-term framework. It does not stipulate specific rules or objectives for fiscal policy but requires that fiscal strategy be framed in accordance with the following principles of sound fiscal management:

- managing financial risks faced by the Australian Government prudently, having regard to economic circumstances, including by maintaining Australian Government general government debt at prudent levels;
- ensuring that fiscal policy contributes to achieving adequate national saving and, as appropriate, moderates cyclical fluctuations in economic activity by taking account of the economic risks the nation faces and their impact on the Australian Government's fiscal position;
- pursuing spending and taxing policies that are consistent with a reasonable degree of stability and predictability in the level of the tax burden;
- maintaining the integrity of the tax system; and
- ensuring that consideration is given to the financial effect of policy decisions on future generations.

Australia's longer-term fiscal sustainability was examined in the Intergenerational Report released as part of the 2002-03 Budget. This report raised awareness of the potential long-term fiscal pressures facing the Australian Government arising from ageing of the population and projected strong rises in Australian Government health expenditures. In particular, the Intergenerational Report projected a gap between the level of government spending and revenues of around 5 per cent of GDP by 2042. Recently, the Government released the discussion paper, *Australia's Demographic Challenges*, which discussed policy challenges in light of the fiscal pressures highlighted in the Intergenerational Report.

Low public debt

The Government's fiscal strategy ensures that the current low levels of Australian Government general government net debt will be maintained through time and will fall as a share of GDP.

- The Government will have successfully reduced Australian Government general government net debt by around $70 billion, from 19 per cent of GDP in 1995-96 to around 3.2 per cent of GDP in 2003-04. This fall is due to a combination of accumulated cash surpluses and proceeds from the sale of financial assets.

- Good fiscal management has meant that the Government has been able to deliver tax cuts and priority spending without the need to borrow in net terms. This ensures that the fiscal position is sound and sustainable.

- Australia now has one of the lowest levels of general government net debt in the OECD. Unlike countries such as the United States, Japan and Germany, which are running up debt, Australia's net debt is falling. This places Australia in a relatively better position than many other countries to respond to future economic shocks.

PART 2
FISCAL AND ECONOMIC OUTLOOK

This part presents the main budget aggregates for the 2004-05 Budget and reconciles these with estimates from the 2003-04 MYEFO. It includes the budget financial statements and outlines the sensitivity of the budget estimates to the uncertainty of the economic parameters.

More detail on budget revenue and expenses is included in Statements 5 and 6.

This part also discusses the performance of the labour market in recent decades, the changes to policy settings that have contributed to improved performance in recent years, and the scope for policy settings to be tuned to further reduce unemployment.

STATEMENT 2: FISCAL OUTLOOK

This statement summarises the main budget aggregates for the Australian Government general government sector.

The fiscal outlook for the Australian Government remains positive, with an underlying cash surplus of $2.4 billion. Across the forward estimates period, the Government has maintained the budget in surplus after providing for its *More help for families* package comprising $19.2 billion in new assistance to families, $14.7 billion in structural tax reform, and $2.7 billion in incentives for saving for retirement.

Further reductions in net debt over the forward years are expected as the budget remains in surplus.

STATEMENT 2: FISCAL OUTLOOK

The fiscal outlook for the Australian Government remains positive, with an underlying cash surplus projected in 2004-05. Across the forward estimates period, the Government has maintained the budget in surplus after providing for its *More help for families* package comprising $19.2 billion in new assistance to families, $14.7 billion in structural tax reform, and $2.7 billion in incentives for saving for retirement.

BUDGET AGGREGATES

An underlying cash surplus of $2.4 billion is estimated for 2004-05, compared to $3.8 billion at the *Mid-Year Economic and Fiscal Outlook 2003-04* (MYEFO). Underlying cash surpluses are projected to continue across the forward estimates.

In accrual terms, a fiscal surplus in 2004-05 of $0.7 billion is now forecast compared to $1.6 billion at MYEFO. Fiscal surpluses are expected to continue across the forward estimates.

Table 1: Australian Government general government sector budget aggregates(a)

	Actual	Estimates		Projections		
	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Revenue ($b)	**175.0**	**186.2**	**193.2**	**201.4**	**212.2**	**223.1**
Per cent of GDP	23.2	23.0	22.5	22.2	22.2	22.1
Expenses ($b)	**169.2**	**183.1**	**192.3**	**200.6**	**210.0**	**220.9**
Per cent of GDP	22.4	22.6	22.4	22.1	22.0	21.9
Net operating balance ($b)	5.8	3.1	0.8	0.8	2.2	2.2
Net capital investment ($b)	-0.2	0.0	0.1	0.0	-0.1	-0.4
Fiscal balance ($b)	**6.0**	**3.0**	**0.7**	**0.7**	**2.3**	**2.6**
Per cent of GDP	0.8	0.4	0.1	0.1	0.2	0.3
Underlying cash balance ($b)	**7.5**	**4.6**	**2.4**	**1.6**	**3.4**	**4.5**
Per cent of GDP	1.0	0.6	0.3	0.2	0.4	0.4
Memorandum item:						
Headline cash balance ($b)	7.3	4.0	1.0	0.0	12.8	13.7

(a) All estimates are based on Government Finance Statistics (GFS) standards, but with goods and services tax (GST) revenue collected on behalf of the States and Territories netted off revenue and expenses.

VARIATIONS TO THE FISCAL BALANCE ESTIMATES

The downward revision of $0.9 billion in the 2004-05 fiscal surplus since MYEFO largely reflects the impact of the Government's *More help for families* package ($5.3 billion in 2004-05) and other policy initiatives, partly offset by higher than expected revenue from companies, superannuation funds and income tax withholding.

Table 2 provides a reconciliation of the fiscal balance estimates between the 2003-04 Budget, the 2003-04 MYEFO and the 2004-05 Budget.

Table 2: Reconciliation of 2003-04 Budget, 2003-04 MYEFO and 2004-05 Budget fiscal balance estimates[(a)]

	2003-04 $m	2004-05 $m	2005-06 $m	2006-07 $m
2003-04 Budget fiscal balance	**711**	**-1,148**	**324**	**2,812**
Per cent of GDP	0.1	-0.1	0.0	0.3
Changes between 2003-04 Budget and MYEFO				
Effect of policy decisions(b)				
Revenue	-13	55	207	164
Expenses	1,005	1,461	1,224	1,285
Net capital investment	45	18	-3	-3
Total policy decisions	-1,063	-1,423	-1,014	-1,117
Effect of parameter and other variations				
Revenue	4,343	3,768	5,103	5,586
Expenses	-178	-410	638	999
Net capital investment	168	48	130	250
Total parameter and other variations	4,354	4,130	4,335	4,337
2003-04 MYEFO fiscal balance	**4,002**	**1,558**	**3,645**	**6,032**
Per cent of GDP	0.5	0.2	0.4	0.6
Changes between MYEFO and 2004-05 Budget				
Effect of policy decisions(b)				
Revenue	0	-1,796	-3,883	-4,587
Expenses	5,969	6,209	6,835	7,766
Net capital investment	169	189	151	45
Total policy decisions	-6,139	-8,194	-10,869	-12,398
Effect of parameter and other variations				
Revenue	3,542	6,133	5,712	6,321
Expenses	-1,691	-1,475	-2,248	-2,368
Net capital investment	53	274	24	31
Total parameter and other variations	5,180	7,334	7,936	8,658
2004-05 Budget fiscal balance	**3,044**	**698**	**712**	**2,291**
Per cent of GDP	0.4	0.1	0.1	0.2

(a) A positive number for revenue indicates an increase in the fiscal balance, while a positive number for expenses and net capital investment indicates a decrease in the fiscal balance.
(b) Excluding the public debt net interest effect of policy measures.

Variations in revenue estimates

Total revenue for 2004-05 has been revised up by $4.3 billion since MYEFO. This is largely a consequence of a strong parameter-driven increase in expected revenue from companies, superannuation funds and also income tax withholding partly offset by lower than expected customs duty.

Total tax revenue in 2004-05 has increased by $4.2 billion since MYEFO.

- Income tax withholding has been increased by $720 million, reflecting solid wages growth on top of strong employment and the introduction of the first round of income tax cuts commencing on 1 July 2004.

- Company tax revenue has been revised up by $1.8 billion, reflecting a stronger outlook for company profits.

- Superannuation contributions and earnings taxation revenue has been revised up by $930 million. However, the one-off impact of the Government's decision to extinguish its liabilities to the Telstra and Australia Post superannuation schemes with a payment of $4.6 billion accounts for $610 million of this increase.

- Customs duty revenue has been revised down by $490 million, reflecting the impact of the higher exchange rate on the price of imports as well as tariff reductions under the Australia-United States Free Trade Agreement.

- Other individuals revenue has been revised up by $170 million, reflecting higher profitability of small business enterprises.

- Petroleum excise revenue had been revised up by $250 million, reflecting a higher crude oil price.

Policy decisions taken since the 2003-04 MYEFO are expected to reduce revenue by around $1.8 billion in 2004-05 and around $3.9 billion in 2005-06. The major policy decisions impacting on revenue over the four year period 2004-05 to 2007-08 are outlined below.

- The personal income tax cuts taking effect from 1 July 2004 and 1 July 2005 will reduce tax revenue by $1.9 billion in 2004-05, $3.8 billion in 2005-06, and $14.7 billion over the forward estimates period.

- The further reductions in the superannuation surcharge rate in 2004-05, 2005-06 and 2006-07 will reduce revenue by $610 million over the forward estimates period.

- Additional funding over four years for the Australian Taxation Office for increased compliance activities is expected to result in increased taxation revenue of $251 million in 2004-05 and $1.1 billion over the forward estimates period.

- The Australia-United States Free Trade Agreement, expected to come into force in January 2005, will reduce tariff revenue by $190 million in 2004-05 and around $1.5 billion over the forward estimates period.

- The application of withholding tax to certain payments made to foreign residents will increase taxation revenue by $125 million in 2004-05 and $540 million over the forward estimates period.

- The introduction of a new $1 million threshold of wholesale value for wine producers will reduce wine equalisation tax revenue by $58 million in 2004-05 and $338 million over the forward estimates period.

In 2003-04, revenue has been revised up by $3.5 billion since MYEFO reflecting significantly higher revenue from company tax and improvement in income tax withholding.

More detailed information on revenue can be found in Statement 5. A full description of all policy measures since MYEFO can be found in Budget Paper No. 2, *Budget Measures 2004-05*.

Variations in expense estimates

Since MYEFO, estimated expenses for 2004-05 have increased by $4.7 billion reflecting the impact of new policy decisions of $6.2 billion, partly offset by parameter and other variations of $1.5 billion.

Major new expense policy decisions affecting 2004-05 include $3.4 billion ($19.2 billion over five years) for the Government's *More help for families* package, including:

- $2.5 billion to increase the rate of Family Tax Benefit (A) by $600 per child a year along with a reduction in the income test taper rate;
- $414 million for the relaxation of the income test for Family Tax Benefit (B); and
- $559 million for the introduction from 1 July 2004 of a new Maternity Payment.

Other new policy decisions affecting 2004-05 include:

- $254 million in 2004-05 ($2.2 billion over five years from 2003-04) in additional funding for the *Investing in Australia's Aged Care: More Places, Better Care* package to improve the viability of aged care services and to assist financially disadvantaged residents with their accommodation costs;
- $127 million in 2004-05 ($543 million over the four years) for enhancements to MedicarePlus including improved access to the safety net, the increased bulk-billing incentive and two new Medicare Benefits Schedule items for services provided by allied health professionals and dentists;
- $165 million in 2004-05 for continuing assistance to the Solomon Islands Government for a range of activities including the restoration of law and order and to support broad ranging reforms;
- $157 million in 2004-05 ($612 million over five years from 2003-04) for a range of national security measures under the *Investing in Australia's Security* package;

- $146 million in 2004-05 ($717 million over five years from 2003-04) to the Australian Federal Police to provide management, infrastructure and capacity building assistance to the Royal Papua New Guinea Constabulary; and

- $125 million in 2004-05 ($132 million over three years) for the Australian Defence Force's contribution to Iraqi stabilisation and reconstruction.

In 2004-05, parameter and other revisions have reduced forecast expenses by $1.5 billion, largely reflecting:

- a $426 million reduction in estimated Family Tax Benefit expenses, primarily the result of higher than expected incomes reducing the expected number of recipients eligible for payments;

- a $335 million fall in anticipated Newstart Allowance expenses, largely due to the stronger labour market reducing the expected number of unemployment benefit recipients;

- a $122 million reduction in Child Care Benefit expenses, largely due to an increase in the proportion of outside school care expected to be used, combined with higher than previously forecast incomes of recipients leading to lower than estimated average rates of payment; and

- the regular draw-down of the conservative bias allowance reducing estimated expenses by around $925 million each year from 2004-05.[1]

Offsetting these reductions in estimated expenses in 2004-05 are:

- a $266 million increase in expenses for the Pharmaceutical Benefits Scheme, arising from continued legislative delays by the Senate in passing the proposed increases in the Pharmaceutical Benefits Scheme co-payment measure announced in the 2002-03 Budget;

- a $216 million increase in Defence expenses reflecting the flow on effect of an increase in the non-farm GDP deflator in 2003-04, which is used to index Defence operating expenses; and

- a $183 million increase in personal benefit expenses due to the flow on effect of an upwards revision to forecast Male Total Average Weekly Earnings growth in

---

1 The forward estimates include an allowance for the established tendency of existing government policy (particularly demand driven programmes) to be higher than estimated in the forward years. This allowance known as the conservative bias allowance, is progressively reduced so that the budget year conservative bias allowance is zero by Budget night. The conservative bias allowance is a technique to provide for more reliable forward estimates.

2003-04, reflecting the Government's ongoing commitment to maintain selected pensions at 25 per cent of Male Total Average Weekly Earnings.

In 2003-04, estimated expenses have increased by $4.3 billion since MYEFO. This largely reflects new spending of $6.0 billion in 2003-04 including spending of $2.2 billion for the $600 payment to all Family Tax Benefit (A) eligible families under the *More help for families* package, $513 million for a one-off grant to aged care providers as part of the *Investing in Australia's Aged Care: More Places, Better Care* package, $255 million for a one-off lump sum payment to eligible carers, and a $450 million grant to Australian Rail Track Corporation under AusLink.

This new spending in 2003-04 is partly offset by a reduction in Defence expenses of $500 million resulting from the reallocation of Defence Capability Plan expenditure to beyond the forward years, a reduction in Budget Balancing Assistance to the States of $327 million reflecting increased GST receipts, and a $307 million reduction in drought assistance, largely reflecting lower than anticipated expenditure on Exceptional Circumstances interest rate relief. These variations have been partly offset by the regular draw-down of the provision for underspends.

More detailed information on expenses can be found in Statement 6. A full description of all policy measures since the MYEFO can be found in Budget Paper No. 2, *Budget Measures 2004-05*.

Variations in net capital investment estimates

In 2004-05, forecast net capital investment has increased by $463 million since the 2003-04 MYEFO. This increase represents the combined effect of:

- new policy decisions of $189 million, including $85 million for national security measures under the *Investing in Australia's Security* package, $39 million for the refurbishment of Anzac Park East and West, and $20 million for the redevelopment of detention facilities at Villawood and Maribrynong and the upgrade of the Baxter facility; and

- parameter and other variations of $274 million, largely due to a projected increase in net housing investment by the Defence Housing Authority, reflecting higher than expected demand from defence personnel.

In 2003-04, estimated net capital investment has increased by $222 million, largely reflecting $114 million in capital funding to ensure Australia's preparedness to protect against the threat of Avian flu.

More detailed information on net capital investment can be found in Statement 6. A full description of all policy measures since the MYEFO can be found in Budget Paper No. 2, *Budget Measures 2004-05*.

CASH FLOWS

In 2004-05, an underlying cash surplus of $2.4 billion is now expected, compared with the MYEFO estimate of $3.8 billion. The change in 2004-05 is largely due to the same variations as those impacting on the fiscal balance. The estimated underlying cash surplus for 2003-04 remains largely unchanged while the underlying cash surpluses for the forward estimates have been revised downwards.

Table 3 provides a summary of Australian Government general government sector cash flows.

Table 3: Summary of Australian Government general government sector cash flows(a)

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$b	$b	$b	$b	$b
Cash receipts					
Operating cash receipts	184.1	193.4	201.2	211.3	222.3
Capital cash receipts(b)	1.1	0.8	0.6	0.5	0.5
Total cash receipts	185.2	194.2	201.8	211.8	222.7
Cash payments					
Operating cash payments	178.0	188.9	197.3	205.9	215.9
Capital cash payments(c)	2.6	2.9	2.9	2.5	2.3
Total cash payments	180.6	191.8	200.2	208.4	218.2
Finance leases and similar arrangements(d)	0.0	0.0	0.0	0.0	0.0
Underlying cash balance	**4.6**	**2.4**	**1.6**	**3.4**	**4.5**
Per cent of GDP	0.6	0.3	0.2	0.4	0.4
Memorandum items:					
Net cash flows from investments in financial assets for policy purposes(e)	-0.6	-1.4	-1.6	9.4	9.2
Headline cash balance	**4.0**	**1.0**	**0.0**	**12.8**	**13.7**

(a) Cash flows are derived from the accrual GFS framework excluding GST.
(b) Equivalent to cash receipts from the sale of non-financial assets in the GFS cash flow statement.
(c) Equivalent to cash payments for purchases of new and second-hand non-financial assets in the GFS cash flow statement.
(d) The acquisition of assets under finance leases decreases the underlying cash balance. The disposal of assets previously held under finance leases increases the underlying cash balance.
(e) Under the cash budgeting framework, these cash flows were referred to as 'net advances'.

Table 4 provides a reconciliation of the variations in the underlying cash balance estimates.

Table 4: Reconciliation of Australian Government general government sector underlying cash balance estimates

	2003-04	2004-05	2005-06	2006-07
	$m	$m	$m	$m
2003-04 Budget underlying cash balance	**2,172**	**1,325**	**1,235**	**4,668**
Changes from 2003-04 Budget to MYEFO				
Effect of policy decisions(a)	-1,012	-1,116	-738	-833
Effect of parameter and other variations	3,475	3,621	4,110	3,897
Total variations	**2,463**	**2,504**	**3,372**	**3,064**
2003-04 MYEFO underlying cash balance	**4,635**	**3,829**	**4,608**	**7,733**
Changes from MYEFO to 2004-05 Budget				
Effect of policy decisions(a)	-4,255	-8,271	-11,055	-12,429
Effect of parameter and other variations	4,206	6,832	8,035	8,135
Total variations	**-49**	**-1,439**	**-3,020**	**-4,294**
2004-05 Budget underlying cash balance	**4,586**	**2,391**	**1,587**	**3,438**

(a) Excludes the public debt net interest effect of policy measures.

While the 2004-05 underlying cash balance has decreased by $1.4 billion since the MYEFO, the estimated fiscal balance has decreased by only $0.9 billion. This difference primarily reflects a $0.8 billion increase in accrual taxation revenue relative to taxation receipts due to a reassessment of the expected level of taxation liabilities identified but not expected to be received in 2004-05.

Headline cash balance

A headline cash surplus of $1.0 billion is now forecast for 2004-05 compared with a surplus of $2.9 billion expected at MYEFO. The decrease in the headline cash surplus estimate since MYEFO largely reflects the decrease in the underlying cash balance.

In addition to the lower estimated underlying cash surpluses, the headline cash balance estimate for 2005-06 is reduced compared to MYEFO because of postponement in the expected sale of the Australian Government's remaining shareholding in Telstra.

NET DEBT AND NET WORTH

With the budget remaining in cash surplus in 2004-05 and the forward years, further falls in net debt are expected. From its peak of 19.1 per cent of GDP in 1995-96, net debt is estimated to decrease to $24.7 billion (2.9 per cent of GDP) by the end of 2004-05. Net interest payments are also expected to fall over the forward estimates.

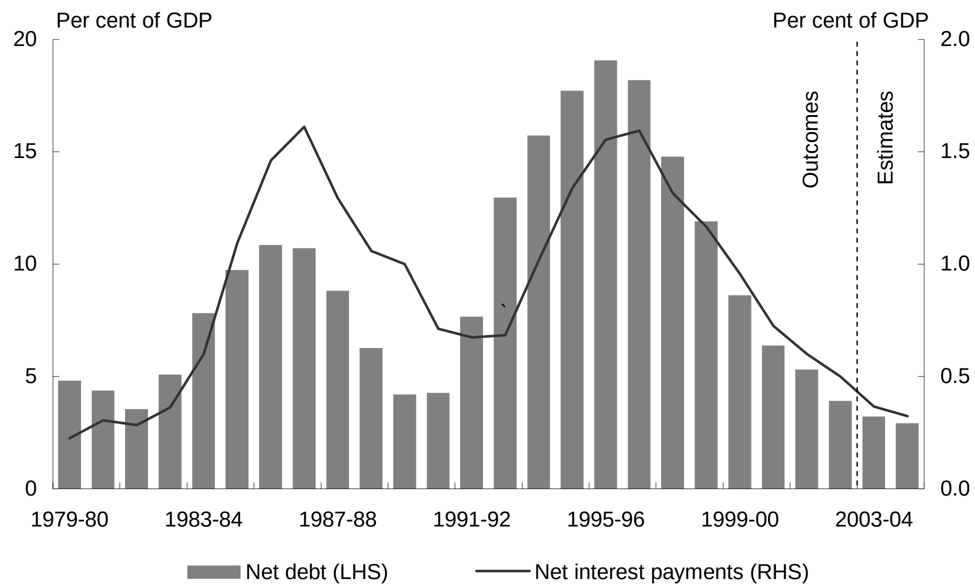
Table 5 and Chart 1 provide a summary of Australian Government general government sector net worth, net debt and net interest payments.

Table 5: Australian Government general government sector net worth, net debt and net interest payments

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$b	$b	$b	$b	$b
Financial assets	104.9	96.2	98.1	92.7	84.5
Non-financial assets	36.8	37.0	37.1	37.1	36.8
Total assets	**141.7**	**133.2**	**135.2**	**129.8**	**121.3**
Total liabilities	**185.3**	**176.1**	**178.1**	**168.3**	**158.8**
Net worth	**-43.5**	**-42.8**	**-42.9**	**-38.5**	**-37.4**
Net debt(a)(b)	**26.0**	**24.7**	**22.3**	**7.4**	**-8.3**
Per cent of GDP	3.2	2.9	2.5	0.8	-0.8
Net interest payments(c)	**3.0**	**2.9**	**3.8**	**2.6**	**1.4**
Per cent of GDP	0.4	0.3	0.4	0.3	0.1

(a) Net debt equals the sum of deposits held, advances received, government securities, loans and other borrowing, minus the sum of cash and deposits, advances paid, and investments, loans and placements.
(b) Includes the impact of the further sale of the Australian Government's shareholdings in Telstra.
(c) Australian Government cash interest payments less cash interest receipts. The 2005-06 projections include the recognition in cash terms of the capital growth on inflation indexed bonds maturing in that year.

Chart 1: Australian Government general government sector net debt and net interest payments



Source: Data are from ABS Cat. No. 5513.0, Australian Government Final Budget Outcomes and Treasury estimates.

Australia's net debt is at low levels and is projected to fall over the forward estimates period. The level of Australia's net debt compares very favourably with other industrialised economies. The ratio of Australia's total general government sector net debt to GDP is among the lowest in the OECD, and is considerably lower than in Europe, Japan and the United States (see Statement 1).

While declining over the forward estimates, the net debt estimates are higher than anticipated at MYEFO. This reflects a deferral in further sales of the Australian Government's shareholding in Telstra, payments to the Telstra Superannuation Scheme in 2003-04 and the Australia Post Superannuation Scheme in 2004-05 to extinguish Australian Government liabilities to the funds, and a reduction in the fiscal profile in 2004-05 to 2006-07.

Having peaked at $8.4 billion in 1996-97, net interest payments are expected to decline to $2.9 billion in 2004-05, representing annual savings in interest payments of around $5.5 billion.

Net worth is expected to improve from -$43.5 billion in 2003-04 to -$37.4 billion in 2007-08, mainly reflecting the cumulative surpluses in the forward estimates.

APPENDIX A: REPORTING STANDARDS

The *Charter of Budget Honesty Act 1998* requires that the budget be based on external reporting standards, and that departures from applicable external reporting standards be identified.

The major external standards used in the budget are the Australian Bureau of Statistics (ABS) accrual Government Finance Statistics (GFS) framework and Australian Accounting Standards (AAS), including Australian Accounting Standard No. 31 *Financial Reporting by Governments* (AAS31).

Budget tables, with the exception of tables in Statement 9, do not include goods and services tax (GST) collections and equivalent payments to the States. Under the *Intergovernmental Agreement on the Reform of Commonwealth State Financial Relations*, all GST receipts are appropriated to the States and Territories and thus are not available for expenditure by the Australian Government. Because the Australian Taxation Office collects GST as an agent for the States and Territories, GST receipts are not shown as Australian Government revenue. Estimates of GST receipts are provided in Table 2 of Statement 8.

The ABS GFS publication (*Australian System of Government Finance Statistics: Concepts, Sources and Methods* Cat. No. 5514.0.55.001 released on 10 October 2003) requires that provisions for bad and doubtful debts be excluded from the balance sheet. This treatment has not been adopted because excluding such provisions would overstate the value of Australian Government assets in the balance sheet (and would, therefore, be inconsistent with the market valuation principle).

The AAS31 financial statements currently record International Monetary Fund (IMF) Special Drawing Rights (SDRs) as a liability. This is consistent with Australian Accounting Standards. The GFS statements also record SDRs as a liability. However, IMF SDRs are not treated as a liability in the ABS accrual GFS publication although they are treated this way in other IMF documentation. In view of these differences, the current approach will remain in place pending further consultation with the ABS and IMF, and developments in train to harmonise GFS and AAS.

Similarly, the GFS financial statements currently adopt the AAS31 financial statements' treatment for circulating coins. Under this treatment revenue is recognised upon the issue of coins and no liability is recorded, as there is no legal obligation requiring coins on issue to be repurchased by the Australian Government. However, in the ABS accrual GFS publication, coins on issue are treated as a liability and no revenue is recognised. This represents a change from that recommended in the previous ABS cash GFS *Concepts, Sources and Methods* publication. The current accounting treatment will remain in place pending further consultation with the ABS and IMF, and developments in train to harmonise GFS and AAS.

The ABS GFS publication also requires defence weapons be treated as expenses. Defence weapons inventories are recorded as capital investment rather than expenses until such inventories can be reliably identified from other defence inventories and measured. The treatment of these inventories as capital or expenses has the same impact on the underlying cash and fiscal balances.

Public access communication assets, computer software and other intangibles are recorded at historic cost, as market value information, or suitable proxies for market value, are not readily observable for these items.

In order to ensure the reporting of reliable AAS and GFS budget estimates and outcomes, taxation revenue is recognised the earlier of when an assessment of a tax liability is made or cash payment is received by the Australian Taxation Office or the Australian Customs Service. Accordingly, for most categories of taxation revenue, there is a short lag between the time at which the underlying economic activity giving rise to the tax liability occurs and when the revenue is recognised. Longer lags of up to a year occur for some elements of company and superannuation funds taxation.

Additional information on the reporting standards and budget concepts is provided in Statement 8.

APPENDIX B: BUDGET FINANCIAL STATEMENTS

The budget financial statements consist of an operating statement, balance sheet, cash flow statement and statement of other economic flows (reconciliation of net worth) for the Australian Government general government sector. The budget financial statements are based on GFS Standards with the exception of the divergences discussed in Appendix A.

Table B1: Australian Government general government sector operating statement

	2003-04 $m	2004-05 $m	2005-06 $m	2006-07 $m	2007-08 $m
Revenue					
Taxation revenue	174,082	182,580	190,377	200,565	211,142
Current grants and subsidies	0	0	0	0	0
Sales of goods and services	4,192	4,266	4,404	4,537	4,615
Interest income	1,244	1,082	1,049	1,682	2,556
Dividend income	4,171	2,570	2,879	2,756	2,144
Other	2,507	2,653	2,675	2,660	2,672
Total revenue	**186,197**	**193,151**	**201,383**	**212,199**	**223,129**
Expenses					
Gross operating expenses					
Depreciation	1,593	1,933	2,130	2,195	2,254
Superannuation	1,946	2,213	2,162	2,101	2,160
Salaries and wages	11,989	12,011	12,408	12,705	12,833
Payment for supply of goods and services	40,014	43,330	44,282	46,302	48,941
Other operating expenses	2,312	2,443	2,419	2,418	2,412
Total gross operating expenses	*57,854*	*61,929*	*63,400*	*65,720*	*68,600*
Nominal superannuation interest expense	5,155	4,702	5,322	5,446	5,673
Other interest expenses	4,248	4,121	3,844	3,773	3,816
Other property expenses	0	0	0	0	0
Current transfers					
Grant expenses	34,634	37,083	37,872	38,802	40,315
Subsidy expenses	5,643	6,064	6,260	6,362	6,571
Personal benefit payments in cash	72,511	74,986	80,687	86,446	92,401
Other current transfers	0	0	0	0	0
Total current transfers	*112,788*	*118,133*	*124,819*	*131,610*	*139,287*
Capital transfers	3,091	3,421	3,240	3,485	3,562
Total expenses	**183,136**	**192,306**	**200,626**	**210,033**	**220,939**
Net operating balance	**3,061**	**846**	**758**	**2,167**	**2,190**
Net acquisition of non-financial assets					
Purchases of non-financial assets	2,618	2,856	2,705	2,549	2,363
less Sales of non-financial assets	879	727	642	484	484
less Depreciation	1,593	1,933	2,130	2,195	2,254
plus Change in inventories	106	-42	-69	21	4
plus Other movements in non-financial assets	-235	-6	182	-16	-58
Total net acquisition of non-financial assets	**18**	**148**	**45**	**-125**	**-429**
Net lending/fiscal balance(a)	**3,044**	**698**	**712**	**2,291**	**2,619**

(a) The term fiscal balance is not used by the ABS.

Table B2: Australian Government general government sector balance sheet

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Assets					
Financial assets					
Cash and deposits	1,607	1,553	1,492	1,315	982
Advances paid	19,027	20,408	21,440	22,824	24,587
Investments, loans and placements(a)	19,668	8,756	8,722	8,717	8,759
Other non-equity assets	17,541	17,881	18,768	20,317	21,926
Equity(b)	47,061	47,636	47,632	39,555	28,275
Total financial assets	*104,905*	*96,234*	*98,055*	*92,728*	*84,529*
Non-financial assets					
Land	4,576	4,410	4,410	4,491	4,536
Buildings (excluding heritage)	13,417	13,377	13,483	13,535	13,589
Plant, equipment and infrastructure(c)	7,951	8,227	8,348	8,236	7,932
Inventories	4,237	4,195	4,126	4,146	4,150
Heritage and cultural assets(c)	4,949	4,950	4,953	4,956	4,957
Other non-financial assets	1,714	1,842	1,812	1,726	1,623
Total non-financial assets	*36,844*	*37,000*	*37,131*	*37,090*	*36,788*
Total assets	**141,749**	**133,234**	**135,185**	**129,818**	**121,317**
Liabilities					
Deposits held	325	325	325	325	325
Advances received	0	0	0	0	0
Government securities(a)	60,555	49,894	48,637	35,159	21,050
Loans	5,271	5,055	4,882	4,717	4,593
Other borrowing	175	138	100	89	54
Superannuation liability	87,869	89,007	92,157	95,226	98,545
Other employee entitlements and provisions	8,426	8,338	8,457	8,592	8,716
Other non-equity liabilities	22,672	23,311	23,554	24,225	25,466
Total liabilities	**185,294**	**176,069**	**178,111**	**168,333**	**158,750**
Net worth(d)	**-43,545**	**-42,836**	**-42,926**	**-38,515**	**-37,434**
Net debt(e)	26,024	24,696	22,289	7,435	-8,306

(a) For 2004-05 and the forward years, transactions relating to debt management activities in *Assets — Investments, Loans and Placements* and *Liabilities — Government Securities* have been netted. This treatment has been applied because of the uncertainty associated with the actual split between government securities and financial assets acquired for debt management purposes.

(b) Equity includes the valuation of the Telstra shareholding, which is valued at the average of the daily share price over a 90-day period, except in the sale years where the valuation is based on the expected sale price.

(c) Heritage and cultural assets were previously included in plant, equipment and infrastructure.

(d) Net worth is calculated as total assets minus total liabilities.

(e) Net debt equals the sum of deposits held, advances received, government securities, loans and other borrowings, minus the sum of cash and deposits, advances paid and investments, loans and placements.

Table B3: Australian Government general government sector cash flow statement[a]

	2003-04 $m	2004-05 $m	2005-06 $m	2006-07 $m	2007-08 $m
Cash receipts from operating activities					
Taxes received	170,544	179,663	187,480	197,381	207,864
Receipts from sales of goods and services	4,342	4,433	4,578	4,703	4,790
Grants and subsidies received	0	0	0	0	0
Interest receipts	1,132	1,014	838	1,357	2,197
Dividends	3,207	3,214	3,199	2,756	2,144
GST input credits received by general government	2,461	2,653	2,629	2,714	2,841
Other receipts	2,417	2,455	2,459	2,432	2,426
Total receipts	**184,102**	**193,433**	**201,183**	**211,343**	**222,261**
Cash payments for operating activities					
Payments for goods and services	-44,041	-47,276	-48,098	-50,295	-53,086
Grants and subsidies paid	-41,793	-44,775	-46,040	-47,276	-48,966
Interest paid	-4,113	-3,888	-4,658	-3,917	-3,598
Personal benefit payments	-70,694	-75,246	-80,625	-86,007	-91,778
Salaries, wages and other entitlements	-16,768	-16,593	-16,602	-17,182	-17,367
GST payments by general government to taxation authority	-129	-131	-132	-138	-141
Other payments for operating activities	-499	-1,013	-1,194	-1,041	-1,004
Total payments	**-178,037**	**-188,922**	**-197,350**	**-205,855**	**-215,939**
Net cash flows from operating activities	**6,065**	**4,511**	**3,833**	**5,487**	**6,322**
Cash flows from investments in non-financial assets					
Sales of non-financial assets	1,112	804	647	489	487
Purchases of new and secondhand non-financial assets	-2,594	-2,917	-2,887	-2,509	-2,304
Net cash flows from investments in non-financial assets	**-1,482**	**-2,113**	**-2,240**	**-2,020**	**-1,817**
Net cash flows from investments in financial assets for policy purposes	**-599**	**-1,374**	**-1,560**	**9,395**	**9,230**
Cash flows from investments in financial assets for liquidity purposes					
Increase in investments	-70	-41	10	31	-21
Net cash flows from investments in financial assets for liquidity purposes	**-70**	**-41**	**10**	**31**	**-21**
Cash flows from financing activities					
Advances received (net)	0	0	0	0	0
Borrowing (net)	-1,697	315	-514	-13,548	-14,226
Deposits received (net)	-1	0	0	0	0
Other financing (net)	-2,948	-1,352	409	477	179
Net cash flows from financing activities	**-4,645**	**-1,037**	**-105**	**-13,071**	**-14,047**
Net increase/decrease in cash held	**-731**	**-54**	**-61**	**-177**	**-333**
Net cash from operating activities and investments in non-financial assets	**4,583**	**2,398**	**1,594**	**3,468**	**4,505**
Finance leases and similar arrangements(b)	3	-7	-7	-29	-4
Equals underlying cash balance	**4,586**	**2,391**	**1,587**	**3,438**	**4,501**
plus net cash flows from investments in financial assets for policy purposes	-599	-1,374	-1,560	9,395	9,230
Equals headline cash balance	**3,986**	**1,017**	**27**	**12,833**	**13,731**

(a) A positive number denotes a cash inflow; a negative sign denotes a cash outflow.
(b) The acquisition of assets under finance leases decreases the underlying cash balance. The disposal of assets previously held under finance leases increases the underlying cash balance.

Table B4: Australian Government general government sector statement of other economic flows (reconciliation of net worth)

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Opening net worth	**-50,442**	**-43,545**	**-42,836**	**-42,926**	**-38,515**
Opening net worth adjustments(a)	**-891**	**0**	**0**	**0**	**0**
Adjusted opening net worth	**-51,333**	**-43,545**	**-42,836**	**-42,926**	**-38,515**
Change in net worth from operating transactions	**3,061**	**846**	**758**	**2,167**	**2,190**
Change in net worth from other economic flows					
Revaluation of equity(b)	3,210	637	34	3,253	19
Net writedowns of assets (including bad and doubtful debts)(c)	-2,189	-1,347	-1,408	-1,522	-1,627
Assets recognised for the first time(c)	-1	1	3	3	1
Defence weapon platform adjustment(c)	0	0	0	0	0
Liabilities recognised for the first time	0	0	0	0	0
Actuarial revaluations	840	0	0	0	0
Net foreign exchange gains	306	0	0	0	0
Net swap interest received	339	160	168	173	159
Market valuation of debt	1,809	454	304	222	209
Other economic revaluations(c)(d)	412	-42	50	115	130
Total other economic flows	**4,727**	**-136**	**-848**	**2,244**	**-1,108**
Closing net worth	**-43,545**	**-42,836**	**-42,926**	**-38,515**	**-37,434**

(a) Includes the initial recognition of a provision for asbestos related claims. At the time of the *2002-03 Final Budget Outcome* a reliable actuarial measure was not available. Following an actuarial review a provision for asbestos related claims was included in the audited *2002-03 Consolidated Financial Statements*. This liability has now been back-dated to 2002-03.

(b) Revaluations of equity reflects changes in the market valuation of commercial entities, including a change in the value of the Telstra shareholding which is valued at the average daily share price over a 90-day period, except in the sale years where the valuation is based on the expected sale price. This line also reflects any equity revaluations at the point of disposal or sale.

(c) Defence weapons are treated as expenses rather than assets under the GFS framework, hence changes in value do not contribute to net worth and are not included in other economic flows. The adjustment to remove defence weapons has now been reallocated to net writedown of assets, assets recognised for the first time and other economic revaluations.

(d) Largely reflects revaluation of assets and liabilities.

APPENDIX C: SENSITIVITY OF FISCAL AGGREGATES TO ECONOMIC DEVELOPMENTS

A guide to the sensitivity of the forward estimates of expenses and revenue due to variations in economic parameters in 2004-05 is provided in Table C1. It is important to note that the sensitivity analysis gives only a 'rule of thumb' indication of the impact on the budget of changes in prices, wages and other parameters. In each case, the analysis presents the estimated effects of a change in one economic variable only, and does not attempt to capture the linkages between economic variables that characterise changes in the economy more broadly.

Table C1: Sensitivity of fiscal aggregates to changes in economic parameters

	2004-05 $m	2005-06 $m	2006-07 $m	2007-08 $m
Expenses				
Prices	1,190	790	850	880
Wages	110	400	420	450
Unemployment benefit recipients	260	270	280	280
Safety Net Adjustment	30	120	200	280
Revenue				
Prices	50	100	100	100
Wages	1,420	1,520	1,630	1,740
Employment	960	1,030	1,100	1,180
Private final demand	270	280	280	290
Profit	190	300	320	340

Expenses

On the expenses side, the sensitivity analysis of the estimates provides for the following assumptions about changes to four broad groups of parameters. An increase in any of the parameters considered will lead to an increase in expenses, and a decrease in any parameters will lead to a reduction in expenses.

Prices

All price deflators are assumed to change by one percentage point at the start of the September quarter 2004, with wage deflators left unchanged.

- The effect of a change in prices is due to the indexation of Australian Government expenses and a change in the nominal superannuation interest expense.

Wages

All wage and salary growth rates are assumed to change by one percentage point from the beginning of the September quarter 2004, with price deflators left unchanged.

- The effect of a change in wage and salary growth rates is largely due to the Government's commitment to maintain selected pensions at 25 per cent of Male Total Average Weekly Earnings. The wages effect in Table C1 above does not include changes to wage and salary payments in Australian Government departmental expenses.

Unemployment Benefit recipients (includes Newstart Allowance and Unemployed Youth Allowance recipients)

The total number of recipients is assumed to change by five per cent in the Budget year and in all the forward years.

Safety Net Adjustment

The Safety Net Adjustment determined by the Australian Industrial Relations Commission is assumed to change by $2 per week, taking effect from the beginning of the September quarter 2004, and each year after that.

- About $46 billion of expenses, comprising agency departmental expenses, other Australian Government Own Purpose Expenses and Specific Purpose Payments to the States of a departmental expense nature, are indexed to weighted averages of movements in inflation and the Safety Net Adjustment.

- The $30 million figure in the Budget year is lower than in previous years. This is due to the reinstitution of rules preventing post-Budget retrospective adjustments to agencies and programmes funded through annual appropriations.

Revenue

On the revenue side, the sensitivity analysis of the estimates provides for the following assumptions about changes to five broad groups of parameters. An increase in any of the parameters considered will lead to an increase in revenue, and a decrease in any of the parameters will lead to a reduction in revenue.

Prices

All price deflators are assumed to change by one percentage point at the start of the September 2004 quarter, with wage deflators left unchanged.

- A change in prices affects revenue primarily through changes in excise revenue.

Wages

All wage and salary growth rates are assumed to change by one percentage point from the beginning of the September 2004 quarter, with price deflators left unchanged.

- A change in wage and salary growth rates affects revenue through changes in income tax withholding and fringe benefits tax collections.

Employment

The level of employment is assumed to change by one percentage point from the beginning of the September 2004 quarter, with no change in the composition of employment.

- A change in employment affects revenue through increases in income tax withholding collections.

Private final demand

The level of private final demand (consumption plus investment) is assumed to change by one percentage point from the beginning of the September 2004 quarter, with no change in the composition of demand.

- A change in private final demand affects revenue primarily through changes in excise and customs duty collections.

Profits

The level of company profits is assumed to change by one percentage point from the beginning of the September 2004 quarter.

- A change in the level of company profits affects revenue through changes in company tax collections.

STATEMENT 3: ECONOMIC OUTLOOK

This statement presents the economic forecasts that underlie the budget estimates.

STATEMENT 3: ECONOMIC OUTLOOK

The stronger world economy will provide a renewed source of growth for domestic economic activity in 2004-05, leaving Australia well-placed to build on the current economic expansion. Solid economic growth is forecast for 2004-05, with higher export growth largely offsetting lower growth in domestic demand (as measured by gross national expenditure). Employment growth is forecast to remain solid, holding the unemployment rate near 23-year lows, while inflation is forecast to fall to below the bottom of the 2 to 3 per cent target band reflecting moderate growth in labour costs and the higher exchange rate.

OVERVIEW

In 2003-04, **economic growth** in Australia is forecast to be 3¾ per cent, unchanged from the forecasts presented in the *Mid-Year Economic and Fiscal Outlook 2003-04*. Gross national expenditure (GNE) is forecast to grow by 6 per cent for a second consecutive year, with household consumption being boosted by increasing wealth from higher house prices and investment growth driven by increasing construction activity in both the residential and non-residential sectors. Farm production is forecast to grow strongly in 2003-04, contributing ½ of a percentage point to gross domestic product (GDP) growth. Strong consumption growth helped the economy to ride out the challenges presented by the severe drought, a patchy world economy, Severe Acute Respiratory Syndrome (SARS) and continuing international security concerns, which saw net exports make a large detraction from GDP growth in 2003-04.

In 2004-05, economic growth is forecast to be 3½ per cent, with growth in GNE easing to a more sustainable 3¾ per cent, partly offset by a smaller detraction from net exports. Employment is forecast to grow by 1¾ per cent in 2004-05, which should be sufficient to maintain the unemployment rate at around 5¾ per cent. Inflation is forecast to decline to around 1¾ per cent through the year to the June quarter 2005, influenced by low prices for imported consumables and moderate labour cost pressures. The current account deficit is expected to narrow to 5 per cent of GDP in 2004-05, primarily reflecting an improvement in Australia’s terms of trade.

Growth in all of the major components of GNE is forecast to slow in 2004-05. A decline in the construction of medium-density buildings is forecast to contribute to a contraction in dwelling investment activity. Construction of detached housing is also forecast to fall in 2004-05, while investment in alterations and additions is forecast to grow by less than in 2003-04. Growth in household consumption and business investment is forecast to ease towards trend rates in 2004-05, following very strong growth in recent years.

Net exports are forecast to detract ½ of a percentage point from economic growth in 2004-05, as imports continue to grow a little more quickly than exports in response to the still solid levels of domestic spending. Nevertheless, and despite the appreciation of the currency over the past two years, 2004-05 should see a significant improvement in export growth compared with the previous two years. The stronger world economy will provide support for exports of non-rural commodities, manufactures and services. The large grain harvest in 2003-04 has contributed to a build up of farm stocks, which will provide continuing support to rural exports into 2004-05, although the prospect of continuing dry conditions in parts of rural Australia is a risk to the outlook for activity in aggregate.

The recovery in the **world economy** has strengthened significantly since last year's Budget. World growth was strong in the second half of calendar 2003, supported by expansionary monetary and fiscal policy. The durability of the world economic recovery has been aided by the broadening of growth, with strong growth in the United States (US) and East Asia, a firming recovery in Japan and modest growth in Europe.

World economic growth is expected to be brisk throughout 2004, resulting in above trend growth for the year as a whole. Monetary and fiscal policy will likely remain broadly expansionary across a wide group of economies. Despite higher oil and commodity prices, world inflationary pressures are generally low.

In the domestic economy, the very strong growth in **household consumption** expenditure over the past year was supported by robust growth in real after-tax incomes, rapid increases in wealth, and continuing high consumer confidence. These factors, in addition to the Government's Budget initiatives, will continue to support consumption growth in the near term. However, an assumed slower pace of wealth accumulation flowing from a flattening in dwelling prices and slightly lower employment growth are expected to see consumption growth moderate to around 4¼ per cent in 2004-05.

After three years of strong growth, **dwelling investment** is forecast to fall by 3 per cent in 2004-05, with the slowing in activity expected to begin around mid-2004. While the dwelling sector has maintained momentum through 2003-04, the long-anticipated slowdown has begun in some markets, although its extent remains uncertain. Oversupply is most pronounced in pockets of the medium-density sector, particularly for apartments near major city centres. Falls in prices are widely expected and lower construction activity is forecast in this component of the housing sector through 2004-05 and beyond. A more modest downturn is forecast for detached housing, reflecting the relatively more robust conditions in that sector. Partly offsetting the declines in new building activity, renovation work is forecast to continue to grow, but at a slower pace than in recent years.

Growth in **business investment** has been exceptionally strong in recent years, despite the uncertain world environment, but is expected to slow toward trend rates in 2004-05. Business investment conditions remain favourable, with strong profit growth in sectors exposed to the domestic economy, low interest rates, and corporate balance sheets in a generally sound position. Business surveys point to high levels of both business confidence and capacity utilisation.

In line with these positive fundamentals, and supported by lower prices for imported capital goods, new machinery and equipment investment is forecast to grow by 8 per cent in 2004-05. New non-dwelling construction is forecast to grow by 6 per cent in 2004-05 after very strong growth over the past two years. The lower growth forecasts reflect increasing commercial vacancy rates and a slowing in commencements of major new infrastructure projects. However, construction activity is forecast to remain at very high levels as a share of GDP as work on existing projects continues.

While private final demand growth is expected to ease from 6½ per cent in 2003-04 to 4 per cent in 2004-05, growth in **public final demand** is expected to increase from 2¾ per cent to 3½ per cent. Over the past two years, public finances have been supported by strong economic growth, while State government revenues have benefited particularly from activity in the housing market. Economic growth will continue to support the forecast increase in public demand through 2004-05.

Export growth is expected to increase to 8 per cent in 2004-05, reflecting improved conditions in the rural sector and the more positive outlook for the world economy. Increased production capacity in Australia for non-rural commodities is also expected to boost export growth, but the appreciation of the Australian dollar over the past two years will remain a constraint on export growth more generally. **Import** growth is forecast to moderate to 9 per cent in 2004-05, in line with the expected easing in GNE growth. Taken together, the trade forecasts imply that the external sector will detract ½ of a percentage point from economic growth in 2004-05, a significantly smaller detraction than was recorded over the past two years.

The **terms of trade** are forecast to increase strongly in 2004-05, driven by increased prices for a number of Australia's non-rural commodity exports, and further declines in many import prices, particularly for information and communication technology (ICT) goods. This improvement in the terms of trade underpins a forecast narrowing of the current account deficit to 5 per cent of GDP in 2004-05.

Employment growth is forecast to ease slightly to 1½ per cent through the year to the June quarter 2005, reflecting the slight moderation in forecast economic growth for 2004-05. Employment growth at this rate would be sufficient to hold the unemployment rate near 23-year lows of around 5¾ per cent through 2004-05.

The **inflation** outlook remains benign, underpinned by moderate growth in labour costs and the substantial appreciation of the Australian dollar over the past two years. Inflation is forecast to gradually decline to around 1¾ per cent through the year to June 2005, as the effect of the drought on food prices diminishes, the rate of increase in project home prices moderates and the lagged effects of the exchange rate appreciation continued to feed through to retail prices. In addition, tradables prices will benefit from tariff reductions on motor vehicles and textiles, clothing and footwear from 1 January 2005.

The key **risk** to the economic outlook relates to developments in the housing sector, particularly the future path of house prices and the associated wealth effects on consumption. Dwelling investment is forecast to moderate over 2004-05 and the rate of increase in nominal house prices is expected to flatten in aggregate, with some market segments seeing price falls. The assumed slowing in house price growth is forecast to lead to a slowing in household wealth accumulation and consumption growth. However, there is a risk of a more widespread fall in house prices that, if realised, would amplify the slowing in wealth and consumption growth, and have broader implications for aggregate economic activity.

Medium-density apartments, particularly in areas near major city centres, have clearly seen significant over-building in recent years, public warnings of the dangers notwithstanding. A more dramatic fall in prices — even if contained to particular market segments or geographic areas — would introduce additional risk to the outlook.

That said, the dwelling sector has consistently surprised on the upside, and a further boost to aggregate activity from dwelling construction cannot be ruled out.

Increasing levels of household debt also present a potential risk. Household debt-to-income ratios have increased over the past decade, partly in response to low interest rates, moderate rates of inflation and financial market innovation. While there is no evidence that current levels of debt are proving onerous for households in aggregate, higher levels of debt have increased the vulnerability of households to adverse shocks, particularly shocks that might be associated with a deterioration in labour market conditions.

The forecasts are predicated on an assumption that average seasonal conditions will prevail in 2004-05. A continuation of very dry conditions in the south-east, or lower than average seasonal rainfall across broader areas of Australia over the coming year, presents a risk to the prospects for a full recovery in the farm sector and poses a downside risk to the forecasts for farm production and exports in 2004-05.

The risk to the domestic outlook from developments in the world economy appears to have abated significantly since the 2003-04 Budget, with strong growth in the US and East Asia, a firming recovery in Japan and modest growth in Europe. Uncertainties remain, however, about the evolution of the world economic recovery. The recovery has surprised with its strength, suggesting some upside risk to world growth, although questions remain about the unwinding of imbalances in saving and investment flows, and the impact of high and volatile oil prices.

Table 1: Domestic economy forecasts[(a)]

	Outcomes(b) 2002-03 year average	Estimates 2003-04 year average	Forecasts 2004-05 year average	Forecasts Four quarters to June 2005
Panel A - Demand and output(c)				
Household consumption	4.1	5 1/2	4 1/4	4
Private investment				
Dwellings	15.5	6	-3	-5
Total business investment(d)	16.8	11	7	5
Non-dwelling construction(d)	31.9	16	6	-1
Machinery and equipment(d)	16.4	10	8	8
Intangible fixed assets	5.7	4	7	8
Private final demand(d)	6.7	6 1/2	4	3 1/4
Public final demand(d)	4.3	2 3/4	3 1/2	3 3/4
Total final demand	6.2	5 3/4	4	3 1/2
Change in inventories(e)				
Private non-farm	0.1	- 1/4	0	0
Farm and public authorities(f)	-0.1	1/2	- 1/4	1/4
Gross national expenditure	6.2	6	3 3/4	3 1/2
Exports of goods and services	-0.5	2	8	6
Imports of goods and services	13.5	12	9	7
Net exports(e)	-3.0	-2 1/4	- 1/2	- 1/2
Gross domestic product	2.9	3 3/4	3 1/2	3 1/4
Non-farm product	4.0	3 1/4	3 1/2	3 1/4
Farm product	-24.8	20	4	2
Panel B - Other selected economic measures				
External accounts				
Terms of trade	2.1	6 1/2	4 1/2	2 3/4
Current account balance				
$billion	-41.4	-46	-43 1/2	
Percentage of GDP	-5.5	-5 3/4	-5	
Labour market				
Employment (labour force survey basis)	2.5	1 3/4	1 3/4	1 1/2
Unemployment rate (per cent)(g)	6.2	5 3/4	5 3/4	5 3/4
Participation rate (per cent)(g)	63.7	63 1/2	63 1/2	63 1/2
Prices and wages				
Consumer Price Index	3.1	2 1/4	2	1 3/4
Gross non-farm product deflator	2.6	4	2 1/2	1 3/4
Wage Cost Index	3.5	3 3/4	3 3/4	3 3/4

(a) Percentage change on previous year unless otherwise indicated.
(b) Calculated using original data.
(c) Chain volume measures.
(d) Excluding transfers of second-hand assets from the public sector to the private sector.
(e) Percentage point contribution to growth in GDP.
(f) For presentational purposes, forecast changes in inventories held by privatised marketing authorities are included with the inventories of the farm sector and public marketing authorities.
(g) The estimate in the final column is the forecast rate in the June quarter 2005.
Source: Australian Bureau of Statistics (ABS) Cat. No. 5206.0, 5302.0, 6202.0, 6345.0, 6401.0, unpublished ABS data and Treasury.

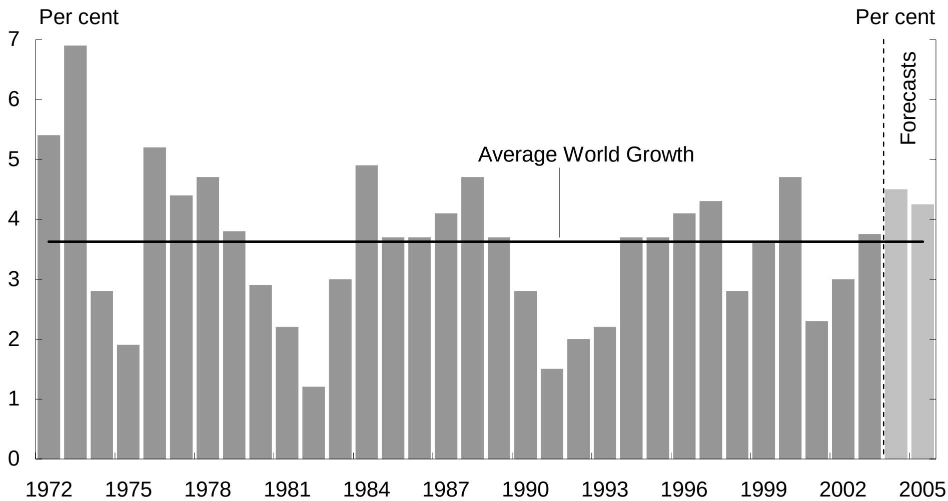
THE OUTLOOK FOR THE INTERNATIONAL ECONOMY

The world economy grew strongly in the second half of 2003, supported by expansionary monetary and fiscal policies. The durability of the economic recovery has been aided by the broadening of growth, with strong growth in the US and East Asia, a firming recovery in Japan, and modest growth in Europe.

World economic growth is expected to be brisk throughout 2004, resulting in above trend growth for the year as a whole. Monetary and fiscal policies are likely to remain broadly expansionary across a wide group of economies. As the world recovery proceeds, policy stimulus is likely to be reduced with economic growth expected to ease accordingly in 2005. Despite a rise in oil and commodity prices, inflationary pressures are generally low reflecting continued excess capacity, with competitive pricing in domestic and world markets.

The world economy grew by 3.9 per cent in 2003 in year-average terms. World GDP is expected to grow by 4½ per cent in 2004, easing to 4¼ per cent in 2005. Growth in Australia's major trading partners is expected to be 4¾ per cent in 2004, before easing back to 4 per cent in 2005.

Chart 1: World GDP growth(a)



(a) World GDP growth rates are calculated using GDP weights based on purchasing power parity.
Source: National statistical publications, International Monetary Fund (IMF) and Treasury.

The risks around the near-term outlook are balanced. An upside risk to the outlook is that the momentum building across large parts of the world economy could generate a more vigorous recovery than is currently envisaged. There were a number of upside surprises to growth over the latter half of 2003 and it could be the case that analysts have been slow to adjust their expectations as the world economy has recovered.

Further, there is a substantial amount of policy stimulus in the pipeline that has the potential to stimulate growth more than anticipated.

Weighing against upside risks are downside risks emanating from geopolitical tensions, current account and fiscal imbalances, and high and volatile oil prices. Recent increases in oil prices reflect strong demand, particularly from China and the rest of East Asia. Increases in oil prices also reflect geopolitical tensions in the Middle East, a desire by the Organization of the Petroleum Exporting Countries (OPEC) to cut production, oil supply disruptions in Venezuela, and low private sector oil stocks, particularly in the US. For some countries, such as those in the euro area, the rise in oil prices has been offset by currency appreciation against the US dollar. However, high oil prices still pose a risk to world growth, with the current drivers of world demand, the US and East Asia, being the regions most negatively affected by higher US dollar oil prices.

The path of adjustment of current account and fiscal imbalances is a key risk to the medium-term outlook. Policy settings in the US and parts of East Asia are highly expansionary and unbalanced world growth has led to large global imbalances. The orderly depreciation of the US dollar and strengthening of domestic demand in East Asia should assist in partly correcting external imbalances. However, this partial adjustment needs to be set against the strong likelihood of imbalances persisting, with ongoing weakness in the euro area and structural impediments to growth in both the euro area and Japan. While the near-term risk of a disorderly adjustment process may have diminished somewhat, risks remain with the possibility of a sharp adjustment to the US dollar and US interest rates if foreign official capital inflows into the US were to be reduced. That said, it is likely that major Asian central banks have provided short-term support to global activity through their purchase of US Government bonds as part of their exchange rate management policies, though there are medium-term costs to these policies that will need to be addressed.

As the world recovery proceeds, interest rates around the world will rise from historical lows as monetary policy becomes less stimulatory. There is also the likelihood that unsustainable fiscal positions will contribute to an increase in global interest rates. Such a scenario would affect not only those countries in which fiscal positions need to be addressed, such as the US, but also emerging market and developing countries. This latter group is at risk of experiencing higher levels of interest rates, and higher spreads against US interest rates, as the recent reduction in risk premia are re-evaluated. An increase in global interest rates could have a large impact on the balance sheets of both the public and private sectors in emerging market and developing countries.

Lack of progress on multilateral trade negotiations and the recent increase in protectionist sentiment in some countries and regions also present a risk to longer-term growth prospects through constraints to increased trade and economic integration. Improving economic conditions, with favourable implications for labour markets in industrialised countries, may act as a countervailing influence. However, the potential for world and domestic imbalances to exacerbate concerns is likely to persist.

Table 2: International GDP growth forecasts(a)(b)

	2000 Actual	2001 Actual	2002 Actual	2003 Actual	2004 Forecast	2005 Forecast
World	4.7	2.4	3.0	3.9	4 1/2	4 1/4
Total OECD	3.9	1.0	1.7	2.2	3 1/2	3
United States	3.7	0.5	2.2	3.1	4 3/4	3 3/4
Japan	2.8	0.4	-0.3	2.7	3	2
Euro area	3.5	1.6	0.9	0.4	1 3/4	2 1/4
Major Trading Partners	5.3	1.6	2.9	3.4	4 3/4	4
Non-Japan East Asia(c)	7.8	2.2	5.0	4.3	6 3/4	5 1/2

(a) Percentage change on previous year.
(b) Growth rates for world and the euro area are calculated using GDP weights based on purchasing power parity, while growth rates for major trading partners and non-Japan East Asia are calculated using export trade weights.
(c) Non-Japan East Asia comprises Korea, Singapore, Taiwan, Hong Kong, China, Indonesia, Malaysia, Thailand and the Philippines.
Source: National statistical publications, IMF and Treasury.

The US economy grew strongly over the second half of 2003 and into 2004. Growth broadened to include a strengthening recovery in business investment and exports, with continued support from consumption. The rebound in business investment over the second half of 2003 was predominantly driven by investment in equipment and software, especially ICT goods. Consumption, particularly of durable goods, was supported by strong growth in disposable incomes, wealth, and a high level of mortgage refinancing triggered by low interest rates. Disposable incomes were boosted by tax rebates, while increases in wealth reflected rising house prices and stronger stock markets.

The near-term outlook for the US economy is for continued strong growth, although not at the rapid pace of late 2003. Investment is expected to be the key driver of growth with productivity, profitability and business confidence all remaining strong. The low cost of capital and the need to replace existing capital equipment should provide further support to investment over 2004. Until recently there were concerns about weak employment growth. These concerns have been reduced somewhat with the release of recent data, which showed a strong rise in employment in the first quarter of 2004.

Despite recent increases in oil and commodity prices, US inflation remains low owing to continued excess capacity in the labour market, strong domestic competitive pressures and little imported inflation. As the recovery continues, monetary policy settings are likely to become less accommodative, as is already reflected in market interest rates. Reflecting these policy settings, US economic growth is expected to remain strong in 2005, but ease gradually as monetary and fiscal stimuli are reduced.

The US current account deficit remains around record high levels, while the size and likely persistence of the fiscal deficit continues to raise concerns about the medium-term outlook for US and world growth. The depreciation of the US dollar will assist in reducing the current account deficit, but in the near term the US current account will likely remain financed by foreign official capital inflows, which heightens US and global vulnerability to shocks and policy changes. A significant strengthening of domestic demand in the rest of the world, combined with a rebalancing of saving and investment within the US, is required before imbalances are likely to be substantially reduced.

The Japanese economy improved markedly over 2003, growing more strongly than expected in the second half of the year. Although concerns about the quality of national accounts data persist, GDP is estimated to have grown by 2.7 per cent in 2003. Growth was driven primarily by exports and business investment, which in turn were driven by external demand and healthier corporate balance sheets. Importantly for the sustainability of the recovery in Japan, consumption also began to contribute to growth.

The 'quantitative easing' monetary policy strategy adopted by the Bank of Japan appears to be having an impact with deflation and deflation expectations easing somewhat. Together with an increase in both consumer and business confidence and growth in disposable incomes, there are positive signs that domestic demand will strengthen in 2004. Improved corporate sector profitability and stronger share prices should support business investment.

Despite the more positive outlook for the Japanese economy, there remain significant structural weaknesses that continue to hamper economic growth. Partly reflecting these concerns and the likely impact of the appreciation of the yen, economic growth is expected to slow in 2005. Looking beyond this, Japan faces significant demographic challenges from a rapidly ageing population. The pressure this will place on the fiscal position is exacerbated by the high levels of government debt. With the Japanese workforce declining, GDP growth will need to come from productivity growth, underlining the urgency of action needed to address structural impediments to growth.

Economies in non-Japan East Asia grew strongly in the second half of 2003. The impact of the SARS epidemic was short but sharp, while avian flu had very little impact on economic growth. The rebound in US growth, particularly the strength of investment in ICT, coupled with very strong growth in China, contributed significantly to export growth across the rest of East Asia. Domestic demand is showing signs of strengthening in the more industrialised East Asian economies, while the developing economies of the region are also growing briskly.

China expanded rapidly in 2003, growing at its highest annual rate since 1996 (Box 1). Output growth was driven by strong investment, particularly in construction and automobiles. Trade has expanded significantly, with vigorous growth in both exports and imports. Rapid money supply and credit growth have raised concerns about the economy overheating and triggered a tightening of policy. A key uncertainty is how effective such tightening will be in reducing strong investment growth and containing inflationary pressures, particularly in the context of its managed exchange rate regime.

The euro area recovery has been hesitant with growth stalling in early 2003, before picking up modestly in late 2003. The improvement in growth was driven by external demand rather than an expansion in domestic demand. The weakness in domestic demand is reflected in the continued low level of consumer confidence. While economic indicators remain mixed, on balance they suggest a continued modest recovery with weakness remaining centred on Germany, which accounts for nearly a third of the output of the single currency zone.

Domestic demand in the euro area remained anaemic despite large fiscal deficits and tax cuts in both Germany and France. In 2004, six euro area countries are expected to breach the 3 per cent of GDP fiscal deficit limit prescribed by the Stability and Growth Pact. Concerns remain about the willingness of euro area governments to tackle their cyclical and persistent structural problems. The pending demographic challenges increase the need for progress on structural reform, particularly while labour movement restrictions from the ten accession countries exist. Europe's capacity to manage macroeconomic policy will be further tested if the accession countries prematurely adopt the euro.

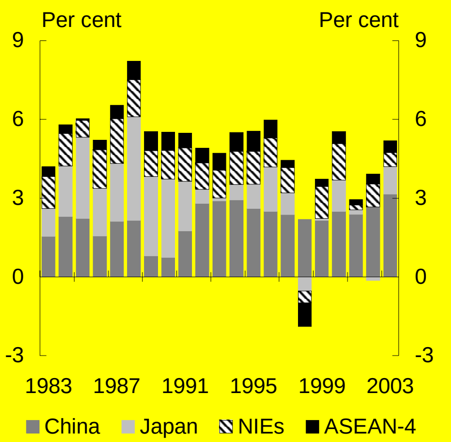
The United Kingdom (UK) grew more strongly than the euro area in 2003 and growth prospects remain significantly better in 2004. Growth in the UK is likely to be underpinned by continued solid consumption growth supported by growth in real disposable incomes and a record low level of unemployment, together with increases in both house prices and financial wealth.

In the near term, the world economic outlook is positive with upside and downside risks broadly balanced. The medium-term outlook presents more challenges, with the adjustment of large current account and fiscal imbalances and significant policy reforms required in many industrialised countries. There are also risks surrounding the related unwinding of the substantial policy stimulus currently in place.

Box 1: China as a driver of regional growth

China's economy has grown by a remarkable 9.7 per cent per year on average over the past twenty years. In more recent years China has made an increasingly important contribution to regional growth (Chart A). China's development as a major regional trading partner has been driven by the opening up of its large markets, its low production cost advantage and East Asian economies seeking out new opportunities. Since mid-2003, the region has exported more to China than to Japan.

Chart A: Contributions to East Asian growth



Source: IMF and Treasury estimates. Newly Industrialised Economies (NIEs) are Korea, Taiwan, Hong Kong and Singapore. ASEAN-4 are Indonesia, Malaysia, Thailand and the Philippines.

China's emergence is also reinforcing East Asia's already strong links with developed economies, particularly the US. China's exports to the US have risen to around 21 per cent of its total exports in 2003, with a considerable portion of these exports including components and semi-finished manufactures from elsewhere in the region.

Despite the considerable momentum in China's economy there are a number of challenges that need to be addressed to ensure the continuation of strong and stable growth.

One challenge is to address possible overheating of the economy. While consumer price inflation has been trending up, it has primarily been driven by food prices, with the prices of many other goods falling. Further, while inflation is likely to edge higher and become more widespread due to producer price pressure, a number of competing factors, such as productivity growth and a large surplus of rural labour, should work together to keep inflation under control.

A greater challenge is to address possible overinvestment. Investment as a share of GDP is now well above its previous peak in 1993, with strong investment in steel, cement, aluminium, property and automobiles. Rapid investment has pushed up commodity prices and placed pressure on infrastructure. There is a risk that capital is being allocated inefficiently and directed towards projects that will prove unprofitable, placing further pressure on China's financial system.

China's policymakers have used a range of measures to rein in money supply and credit growth, including raising banks' required reserve ratios and discouraging loan growth to certain industries. The degree to which these measures are successful will have a large bearing on China's near-term growth path and, by implication, the world economy.

THE OUTLOOK FOR THE DOMESTIC ECONOMY

Key assumptions

The forecasts for the domestic economy are underpinned by several key technical assumptions. The exchange rate is assumed to remain around the average level of recent months (a trade weighted index of around 63). Interest rates are assumed to remain around current levels. World oil prices (West Texas Intermediate) are assumed to fall gradually to around $US32 per barrel by June 2005, broadly in line with market expectations. The farm sector forecasts are based on an assumption of average seasonal conditions in 2004-05.

Deviations from these assumptions can have a material effect on the forecasts. For example, if the exchange rate fell below its assumed level in 2004-05, then it is likely that economic activity and inflation would be higher than forecast, while higher oil prices would likely lead to lower economic activity and higher inflation than forecast.

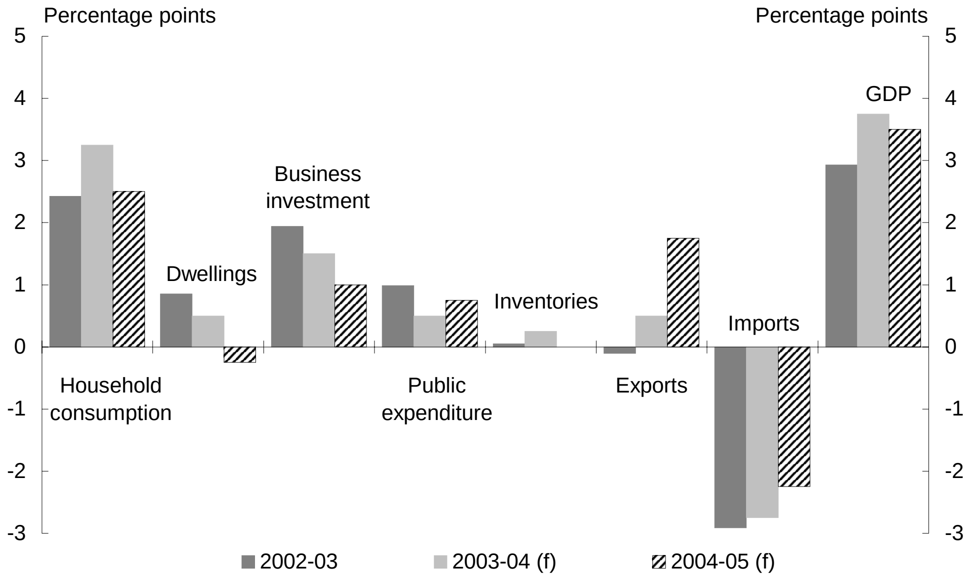
Demand and output

The capacity of the Australian economy to adapt to, and ride out, economic shocks has been reinforced by ongoing economic reforms and prudent macroeconomic policies. Indeed, sustained product and labour market reforms have likely enhanced the effectiveness of macroeconomic policy, while stable macro performance has given firms, employees and consumers the confidence to better pursue opportunities provided by structural reform. That Australia has continued to grow strongly in recent years, despite the challenges presented by drought, an international economic downturn and increasing world security and health concerns, is testament to the increased flexibility and resilience of the economy.

The Australian economy is forecast to grow by 3½ per cent in 2004-05 in year-average terms, slightly below the 3¾ per cent forecast for 2003-04. Growth in non-farm GDP is forecast to pick-up slightly to 3½ per cent in 2004-05, while farm GDP is expected to continue to recover from the drought, increasing by around 4 per cent. Employment growth is forecast to remain solid in 2004-05, with the unemployment rate holding at around 5¾ per cent. Inflation is forecast to fall to around or a little below the bottom of the target band. The current account deficit is forecast to fall to 5 per cent of GDP, primarily reflecting an increase in the terms of trade. Over the past few years, strong domestic growth and weak international demand, combined with a falling supply of rural exports, led to a deterioration in Australia's net export position. As the recovery in the world economy gains strength in 2004-05 and rural production continues to recover, the factors weighing on net exports will abate, leading to a forecast smaller net export detraction from GDP growth.

As a result, the next year should see a rebalancing of economic growth from domestic to external drivers (Chart 2). Slower growth in consumption and business investment and a decline in dwelling investment are forecast to offset an acceleration in public demand growth, leading to a moderation in GNE growth from 6 per cent in 2003-04 to 3¾ per cent in 2004-05. Export growth is forecast to accelerate for the reasons outlined above, while lower growth in domestic spending should lead to a moderation in import growth. Overall, net exports are forecast to detract ½ of a percentage point from economic growth, a substantial improvement from the large detractions seen in recent years.

Chart 2: Contributions to GDP growth(a)

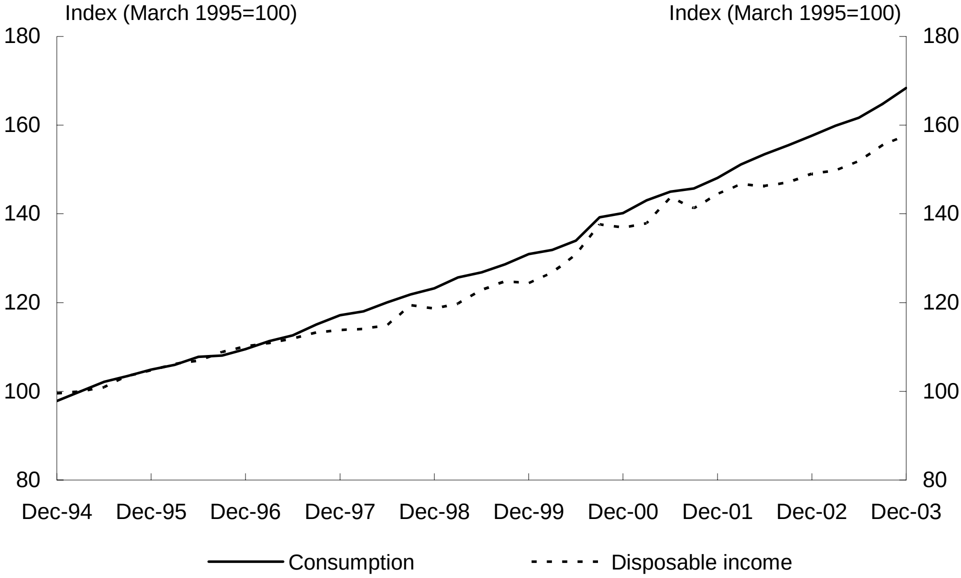


(a) Adjusted for second-hand asset sales.
Source: ABS Cat. No. 5206.0 and Treasury.

Household consumption

Consumption growth has run ahead of income growth for several years (Chart 3), leading to falls in the household saving ratio. Increases in wealth have been an important driver of this stronger consumption growth, with increases in equity prices boosting wealth through the mid to late 1990s and substantial increases in house prices doing the same over the past two years. Access to wealth is also being made easier with the more widespread use by households of mortgage redraw facilities.

Chart 3: Household consumption and disposable income

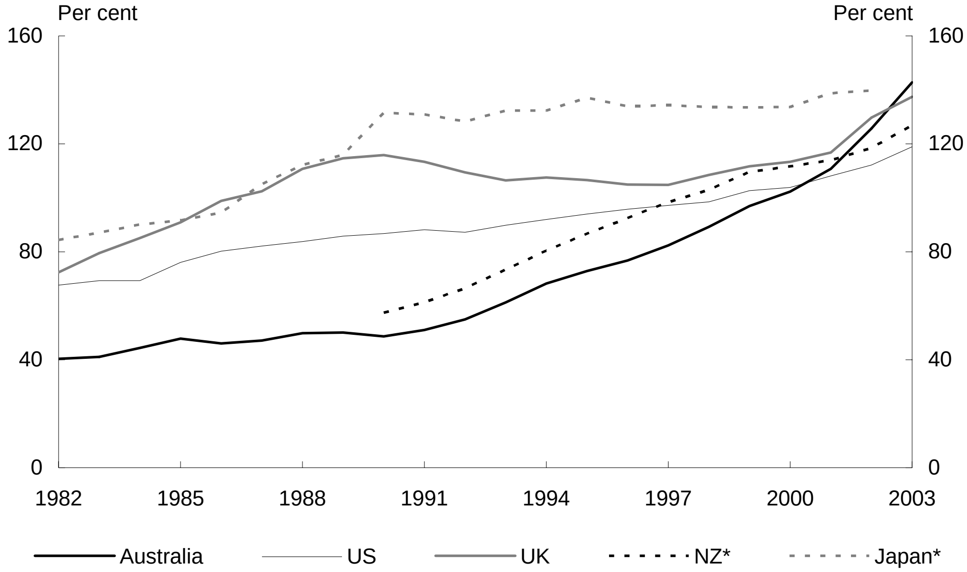


Source: ABS Cat. No. 5206.0.

Developments in the housing sector will be an important determinant of consumption growth over 2004-05. The rate of increase in nominal house prices is expected to flatten in 2004-05, resulting in a significant decrease in the pace of wealth accumulation. This is forecast to reduce consumption growth from the strong rates recorded in 2003-04. However, a more widespread fall in house prices could lead to a sharper than forecast slowing in consumption growth.

The increasing use of mortgage redraw facilities and higher levels of new borrowing for consumption and investment purposes have seen households taking on an increasing level of debt in recent years. This is reflected in Australia's household debt to income ratio, which is now slightly above that prevailing in other similar developed countries (Chart 4). Higher levels of debt have led to a rise in the debt servicing ratio, suggesting that households are now more vulnerable to adverse shocks, particularly those associated with a deterioration in labour market conditions. That said, there is little evidence to suggest that current levels of debt are proving onerous for households in aggregate. The increase in debt has been largely matched by an increase in assets, meaning that households' gearing ratios have remained broadly unchanged. Evidence from the survey of Household Income and Labour Dynamics in Australia (HILDA) indicates that the households with the largest increases in debt are those most able to afford them — that is, high income households.

Chart 4: Household debt to income ratio



* Includes unincorporated enterprises.
Source: ABS Cat. No. 5206.0, 5232.0, Reserve Bank of Australia (RBA) and Treasury.

The pace of consumption growth (Chart 5) is forecast to ease in 2004-05 to 4¼ per cent, below the pace of household disposable income growth.

Recent labour market outcomes have supported consumption growth, with employment increasing solidly over 2003 and the unemployment rate holding near 23-year lows in early 2004. A stronger labour market, combined with moderate growth in wages and the 2003-04 income tax cuts, saw household disposable income growing at a very fast pace in the second half of 2003. Real incomes have also been supported by low consumer price inflation, especially through falling prices for many imported consumables.

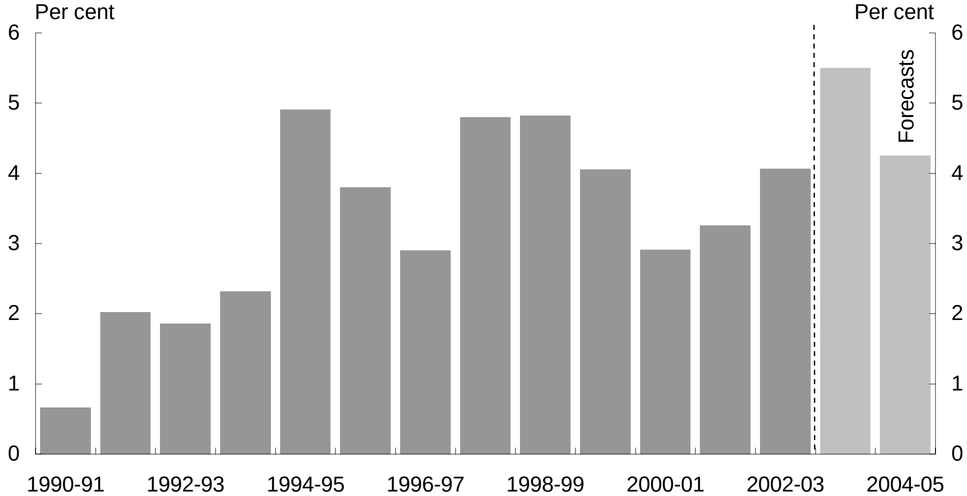
Improved profits from unincorporated businesses, particularly those operating in the retail, construction and farm sectors have also boosted household incomes. However, while farm production has increased following the drought, a higher exchange rate and relatively weak prices for agricultural commodities have prevented farmers' incomes from recovering to their pre-drought levels.

These strong fundamentals have been reflected in surveyed measures of consumer confidence. The Westpac-Melbourne Institute Consumer Sentiment Index has remained at historically high levels, with the interest rate rises of November and December 2003 doing little to dent buoyant confidence levels.

Consumption growth will be supported by solid growth in real household income in 2004-05, underpinned by low consumer price inflation, moderate wages growth and the Government's Budget initiatives. However, the anticipated downturn in dwelling investment should lead to slower growth in the consumption of housing-related durables, following strong growth over the past three years.

A further factor affecting consumption growth over 2004-05 is the path of oil prices. Oil prices have remained high over the past year, reflecting higher energy demand from East Asia, political and security uncertainties in a number of oil-exporting countries and increased discipline on the part of OPEC countries. The higher exchange rate over 2003 dampened the effects of higher US dollar oil prices for Australia. There is a risk, however, that oil prices could increase further or the Australian dollar could fall, causing households to reduce discretionary expenditure to offset an increase in petrol prices.

Chart 5: Growth in household consumption



Source: ABS Cat. No. 5206.0 and Treasury.

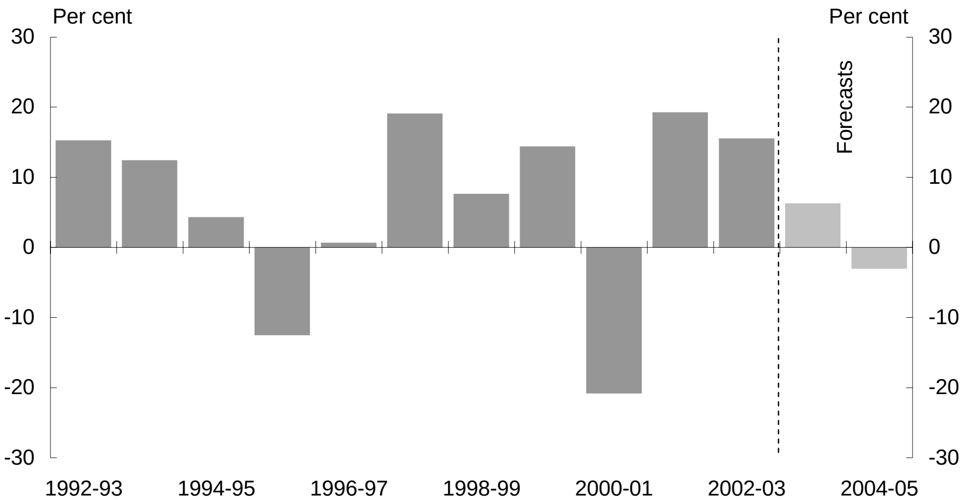
Dwelling investment

Dwelling investment is forecast to fall by 3 per cent in 2004-05, following forecast growth of 6 per cent in 2003-04 (Chart 6). A decline in the construction of medium-density housing and a smaller fall in detached housing should dominate modest growth in alterations and additions in the year ahead. There remains considerable dwelling construction work in the pipeline, which should hold activity in the dwelling sector at high levels in the near term.

Conditions in the detached sector of the housing market have been more restrained than in the medium-density sector. Nevertheless, the lagged effects of higher interest rates and slightly weaker underlying demand are expected to lead to a modest fall in construction activity in 2004-05. Supporting the outlook for a slowing, private sector house approvals have fallen by 11 per cent since September 2003 and finance for new dwellings has also fallen in recent months.

In contrast to conditions in the detached sector, the medium-density sector is presenting much clearer evidence of oversupply, particularly for apartments near major city centres. As a result, a sharp decline in medium-density construction is expected in 2004-05, driven by falling demand by investors who are now facing higher vacancy rates, lower rental yields and increased borrowing costs following the interest rate increases in November and December 2003. In addition, apartment prices in a number of markets have begun falling, raising the prospect of much slower capital gains than in the past or capital losses for some recent investors. At the same time, alternative investments, such as equities, have begun to perform relatively more strongly, which influences the general attractiveness of investment in real estate. Partial indicators are consistent with this outlook, with medium-density approvals falling recently and new investor finance halving since its peak in December 2002.

Chart 6: Growth in dwelling investment



Source: ABS Cat. No. 5206.0 and Treasury.

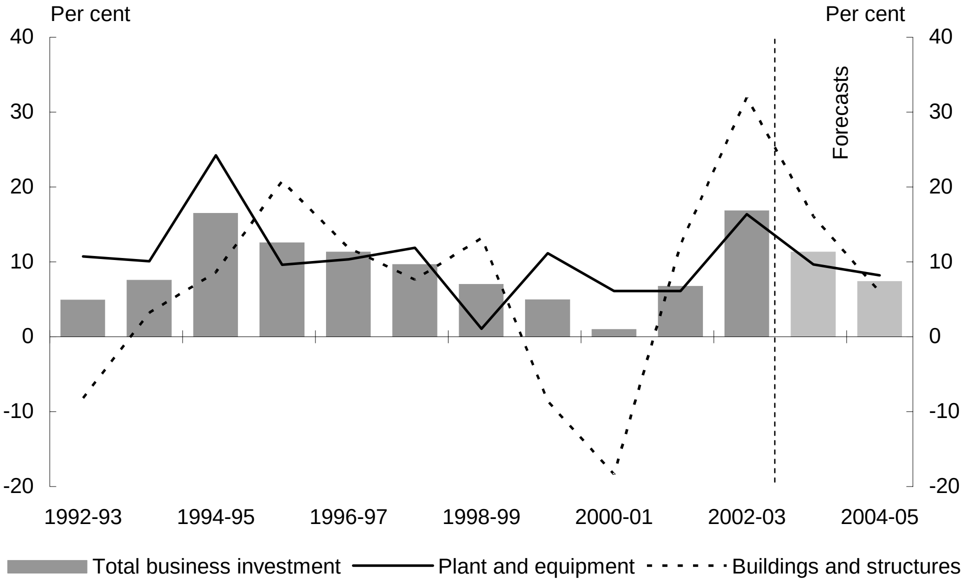
The decline in medium-density construction is expected to be greatest in inner Melbourne and Sydney, where evidence of oversupply is the most pronounced. There is a risk that falling prices in the medium-density sector could prompt a more widespread fall in house prices. This entails a risk for the forecast growth of both consumption and housing investment (see the previous section for a discussion of the effects of changes in wealth on consumption growth).

Alterations and additions remain a relatively cost effective option for owner-occupiers who desire a higher quality dwelling but want to avoid the stamp duties and transaction costs that apply to the purchase of a house or apartment. Investment in alterations and additions is forecast to grow in 2004-05, albeit at a slower pace than in 2003-04, providing some offset to the decline in new dwelling investment. The lower rate of growth in renovation work in 2004-05 reflects the effect of moderating growth in wealth and last year's interest rate rises. The expectation that increases in house prices are likely to be more subdued in 2004-05 will also tend to restrain alterations and additions work by investors seeking capital gains from renovated properties.

Business investment

New business investment is forecast to grow by 7 per cent in 2004-05, following 11 per cent growth in 2003-04 (Chart 7). The fundamental drivers of business investment remain very supportive and, partly as a consequence, business confidence remains at historically high levels. Profits have increased sharply over the past year, strengthening corporate balance sheets, particularly in sectors more exposed to the domestic economy. Interest rates remain at relatively low levels, capacity utilisation is high, domestic demand remains robust and international demand is strengthening.

Chart 7: Growth in business investment[(a)]



(a) Excluding net purchases of second-hand public sector assets by the private sector.
Source: ABS Cat. No. 5206.0 and Treasury.

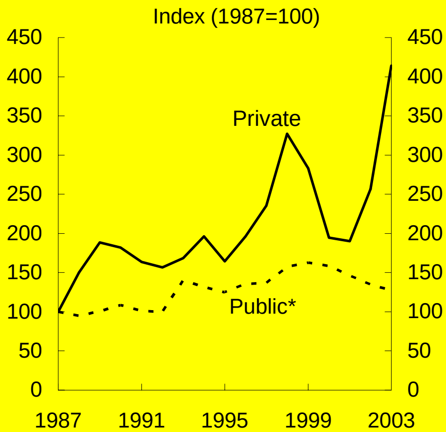
The risk identified in last year's Budget that businesses may scale back discretionary investment expenditure in response to heightened world uncertainty does not appear to have been a significant factor in 2003-04. Indeed, the strength of business investment in the face of world economic and security concerns highlights the confidence of businesses in the Australian economy, which has been complemented by the ongoing low cost of capital.

The mining sector has been an important driver of business investment over the past year as the continued emergence of China and strengthening growth in the international economy has boosted the demand for mineral-related commodities. This is expected to continue into 2004-05. Purchases of aircraft by Australia's major airlines have also continued to support investment spending, although this has been at a lower rate than in 2002-03. The move towards private provision of public-access infrastructure is also boosting private investment for projects that would once have been undertaken by government (Box 2).

Box 2: Infrastructure investment

Private engineering construction has increased sharply in recent years. In fact, new engineering construction by the private sector more than doubled in the three years to the December quarter 2003. A part of this increase reflects the building of public access infrastructure.

Chart A: Road infrastructure construction



* Includes work done by the private sector for the public sector.
Source: ABS Cat. No. 8762.0 and Treasury.

In the past, most public access infrastructure was paid for by the public sector. However, this has been changing in recent years as the private sector has become more involved in the provision and operation of infrastructure facilities. The growth in private engineering construction in recent years has been partly driven by this compositional change from public to private investment spending.

One example of this compositional change is in spending on road infrastructure, where private spending has grown strongly (Chart A). Private Public Partnerships (PPPs) are one vehicle by which private participation in infrastructure provision is increasing. Examples of PPPs include the Lane Cove Tunnel (valued at around $1 billion), the Cross City Tunnel and Westlink M7 Motorway (valued together at over $2 billion) and the Citylink project (valued at around $2 billion).

While vehicles such as PPPs are an increasingly important component of business investment, important public policy issues around the appropriate management and allocation of risks in such projects remain.

Growth in machinery and equipment investment is expected to be 8 per cent in 2004-05. The latest survey of investment intentions indicated that firms' first estimates of nominal spending on machinery and equipment investment in 2004-05 were lower than their first estimates for 2003-04. However, early capital expenditure estimates provide only a broad indication of possible outcomes and, as the year unfolds, it is likely that firms will upgrade their investment intentions more strongly than in recent years as the strength of the recovery in the world economy becomes more apparent. The significant fall in the price of imported machinery and equipment as a result of the appreciation of the exchange rate over the past two years will also support real business investment in 2004-05.

Non-dwelling construction is expected to grow by 6 per cent in 2004-05. The level of engineering construction is expected to remain very high over 2004-05, but growth should pull back from the exceptionally fast rate seen over the past two years. A large number of engineering construction projects remain in the pipeline or underway, including such high value projects as the Bayu Undan gas platform, the North West Shelf expansion, and the Western Sydney Orbital. However, a large part of the work on projects that are currently underway is expected to be completed in 2003-04 and a number of the high value investment projects on the horizon are not expected to see significant expenditure until after 2004-05, leading to a slowing in engineering construction growth over 2004-05.

New building construction is likely to see a moderate cyclical downturn after also experiencing very strong growth in recent years. The latest work-yet-to-be-done data from the Australian Bureau of Statistics suggest that activity in the sector may have peaked. The anticipated slowing in new building construction is also consistent with information from the latest *Delta Electricity Access Economics Investment Monitor*, which points to the absence of large projects scheduled to begin construction in 2004-05. Much of the forecast slowing in activity reflects excess capacity in the commercial office market.

Inventories

In 2004-05, output is expected to broadly keep pace with sales, with inventories making no net contribution to GDP growth. Movements in farm and public authority stocks are forecast to detract ¼ of a percentage point from GDP growth in 2004-05, following a contribution of around ½ of a percentage point in 2003-04. Stronger farm production in 2003-04 initially added to farm and marketing authority stocks, but some of this is likely to be exported in 2004-05.

Public final demand

Public final demand[1] constitutes around 22 per cent of GDP. The final demand of the national public sector (including the final demand of the Australian Government) makes up around 8 per cent of GDP, while the remainder is from the State and local public sector.

Growth in public final demand is forecast to ease slightly, to 2¾ per cent in 2003-04, from the above trend rate of growth observed in 2002-03, before picking up to

1 Public final demand comprises the public sector's expenditure on goods and services. It does not include payments such as personal benefits and other transfers.

3½ per cent in 2004-05. A range of investment projects — particularly at the State and local government level — will continue to support solid growth in public spending in 2004-05.

Developments in the housing market present a particular uncertainty for public finances at the moment. Changes in housing construction activity, real estate turnover and house prices all have the capacity to affect taxation revenue, particularly for the States. As a consequence, public spending decisions could also be affected by developments in these areas.

Net exports and the current account

Net exports

Net exports are forecast to detract ½ of a percentage point from GDP growth in 2004-05. This is a significant expected improvement in the net export performance, following a detraction of more than 5 percentage points from GDP growth over the past two years.

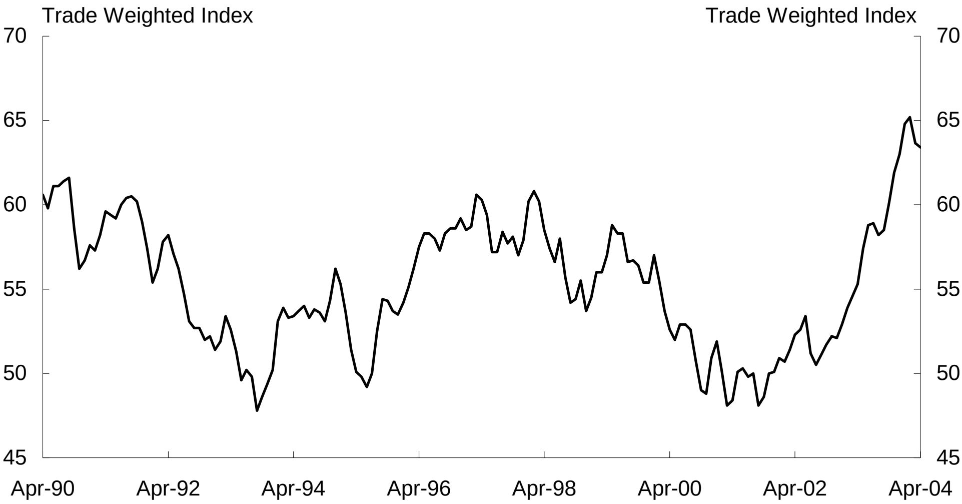
Imports are forecast to increase by 9 per cent in 2004-05, below the 12 per cent growth forecast for 2003-04. Lower growth in imports is consistent with the forecast moderation in GNE growth. However, the appreciation of the exchange rate over the past two years, which has led to a fall in the prices of imported consumption and investment goods, will continue to support import demand over 2004-05.

Exports are forecast to increase by 8 per cent in 2004-05, following only modest growth of 2 per cent in 2003-04. The recovery in exports is expected to be underpinned by the strengthening recovery in world demand, growth in farm production and a pick-up in tourist arrivals. The sharp appreciation of the nominal exchange rate over the past two years will remain a constraint on export growth in the near term (Chart 8). The real exchange rate has appreciated by even more than the nominal exchange rate, reflecting higher rates of inflation in Australia than in our trading partners.

Exports of non-rural commodities, which account for the largest share of Australia's exports, are forecast to grow strongly in 2004-05. This growth is expected to be driven by increased production capacity in Australia, especially for iron ore, coal, and liquefied natural gas, which has been ramped up in response to very strong world demand for bulk commodities, notably from China (Box 3). However, capacity constraints in domestic transport infrastructure, ports and international shipping may restrain export growth in some areas in the near term. The duration and strength of economic growth in the US, Japan and China will be an important determinant of the demand for Australia's non-rural commodity exports.

Rural exports are forecast to grow strongly in 2004-05, in line with the recovery in farm production in 2003-04 from the 2002-03 drought. Weather conditions remain a critical factor for farm production in 2004-05. Irrigated crops and livestock are yet to fully recover from the impact of the drought. In the case of livestock, a full recovery may take some time. Dry conditions in parts of Australia to date in 2004, particularly in the south-east, remain a risk to farm production in the coming year. In the event that Australia was to experience prolonged drought conditions so quickly after the 2002 experience, this would likely have serious implications for aggregate activity and, in particular, for rural and regional Australia.

Chart 8: Exchange rate



Source: RBA.

Exports of elaborately transformed manufactures are forecast to pick up over the course of 2004-05, in line with the strengthening international economy. However, the forecast growth in manufactured exports is expected to be less than in previous recoveries, due to the loss of competitiveness of Australian goods in international markets related to the sharp appreciation of the real exchange rate over the last two years.

Services exports fell sharply in recent years, reflecting the effects on tourism of a weak world economy and heightened global security and health concerns. The SARS outbreak led to a particularly sharp downturn in Australia's inbound tourism. As the world economy continues to recover through 2004-05, services exports are forecast to increase strongly. Nevertheless, people are now more conscious of the potential security and health issues associated with overseas travel, and sentiment is likely to be more sensitive to perceived changes in security conditions.

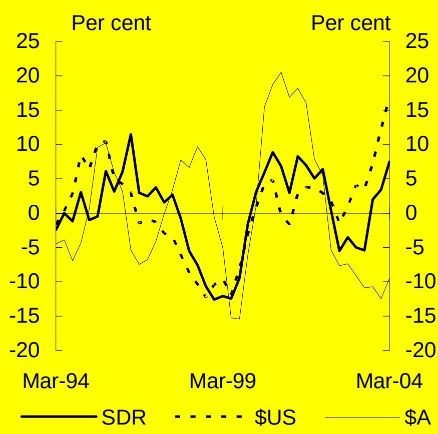
There has also been considerable focus recently on the perceived threat of 'off-shoring' — that is, the provision of services to the Australian market from other countries. However, Australia has traditionally exported and imported services — as with goods — and the transfer of, for example, call centre jobs offshore is no different than the purchase of, for example, legal services from a New York law firm (Box 4).

The critical thing to recognise is that dynamic, flexible economies see the constant creation and loss of jobs, and that maximising competitiveness and productivity are key elements in generating sustainable growth in jobs and living standards. These issues are discussed further in Statement 4.

Box 3: Commodity prices

China's booming economy, as well as the recovery in the US and Japan, has pushed up world demand and prices for non-rural commodities. In particular, the rapid expansion of the Chinese economy — which grew by 9.1 per cent in 2003 — has required vast amounts of raw materials. This has contributed to a rise in non-rural commodity prices of almost 8 per cent through the year to the March quarter 2004 in currency neutral (Special Drawing Rights (SDR)) terms (Chart A).

Chart A: Non-rural commodity prices
(Through the year)



Source: RBA.

Dramatic rises in the price of Australia's bulk commodity exports, such as coal and iron ore, are expected as new contracts with China and Japan come into effect.

Although some of the recent price rises have been partially offset by the appreciation of the Australian dollar, Australian firms are well positioned to take advantage of highly favourable international conditions and the anticipated increases in demand and prices in the period ahead.

In the past two years, capital expenditure by the mining industry has increased dramatically in Australia, consistent with the high levels of profitability in the sector over that period. This expansion in mining capacity can also be seen in mining employment, which grew by 9.2 per cent through the year to the March quarter 2004 to be nearly a third higher than its low in June 2000.

It is expected that the increased capacity will allow non-rural commodities exports to grow by around 9 per cent in 2004-05.

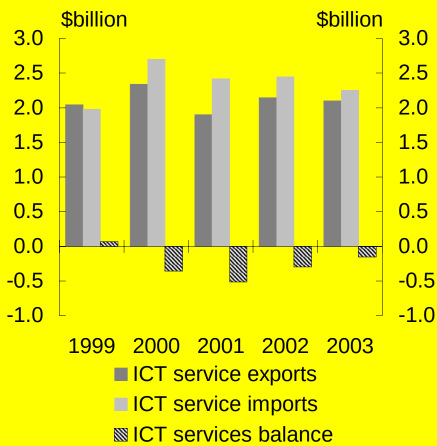
Further export growth may be expected beyond 2004-05. However, it is also expected that price growth will moderate as additional capacity comes on line — both in Australia and internationally. Furthermore, the continuation of the very high demand for non-rural commodities is subject to risks surrounding the sustainability of growth in China and other parts of the world.

Box 4: Recent trends in the trade of services

Australia's current account deficit (CAD) has widened over the past two years. This has largely reflected a widening of the trade deficit, with imports being supported by strong domestic demand and exports subjected to a series of supply and demand shocks (see Box 5).

One trade issue that has become more prominent in recent times is 'off-shoring' — that is, the provision of business services to the Australian market from other countries. The off-shoring of ICT services, such as call centres, has been a particular area of focus.

Chart A: Trade in ICT services



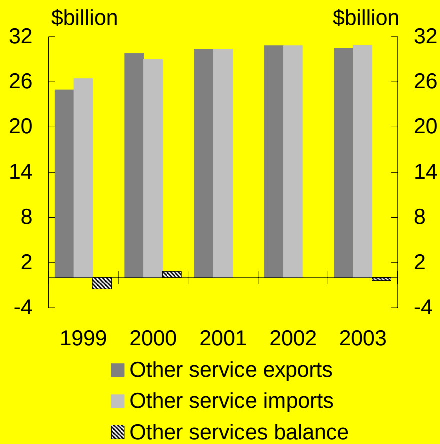
Source: ABS Cat. No. 5302.0.

Trade in ICT services constitutes under 10 per cent of Australia's total trade in services. While Australia runs a deficit in ICT services, the deficit is small and has declined over the past two years (Chart A).

Australia's trade in non-ICT services is also close to balanced and has remained relatively steady in recent years (Chart B).

As a result of this near-balance on the services account, the services deficit only accounted for 1 per cent of the CAD in 2003, despite services constituting around one-fifth of exports and imports. In contrast, the goods deficit accounted for around 50 per cent of the CAD.

Chart B: Trade in non-ICT services



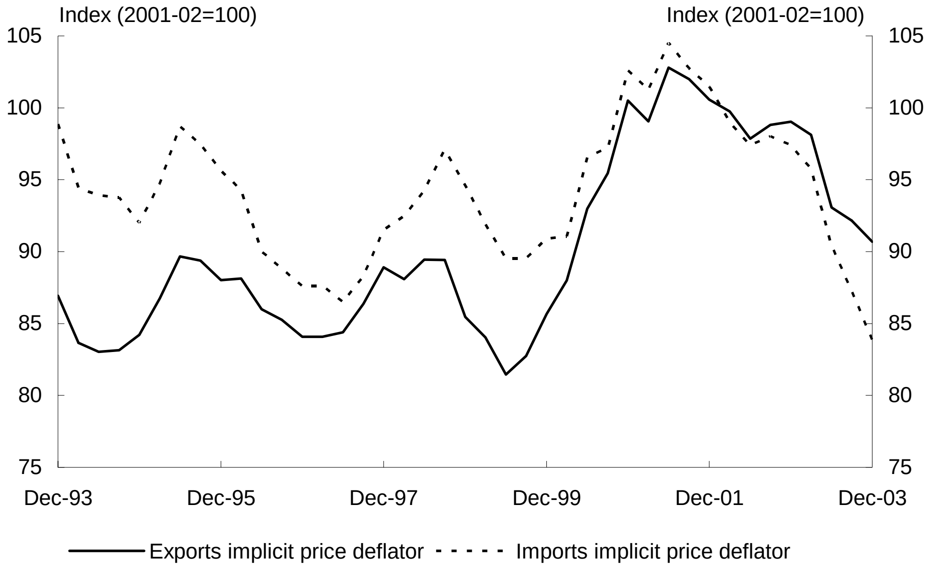
Source: ABS Cat. No. 5302.0.

It is important to recognise that service export industries are significant employers in the Australian economy. While some employment will be lost to off-shoring, the trade data suggest that Australia is also benefiting from employment creation in service export industries.

The terms of trade

The terms of trade are forecast to increase by 4½ per cent in 2004-05, following growth of 6½ per cent in 2003-04. Export prices are forecast to strengthen through 2004-05, particularly for non-rural commodities. The growth in import prices is forecast to remain subdued. Export prices have fallen in recent years, but the fall in import prices has been much greater, providing a boost to the terms of trade (Chart 9).

Chart 9: Export and import prices (AUD)



Source: ABS Cat. No. 5302.0.

As the recovery in the world economy gathers strength, commodity prices are forecast to increase, with energy-intensive manufacturing countries, such as China, making a relatively greater contribution to world growth. Substantial price rises are expected for Australia's bulk commodity exports, with many coal and iron ore contract prices rising significantly after the recent round of international negotiations.

Import prices are forecast to be subdued over 2004-05 following price falls over the past year, which were driven by the sharp rise in the Australian dollar. Technological progress is driving the prices of ICT goods lower on world markets. The increasing contribution of low-wage economies to the world production of manufactures and services is also helping to restrain growth in import prices.

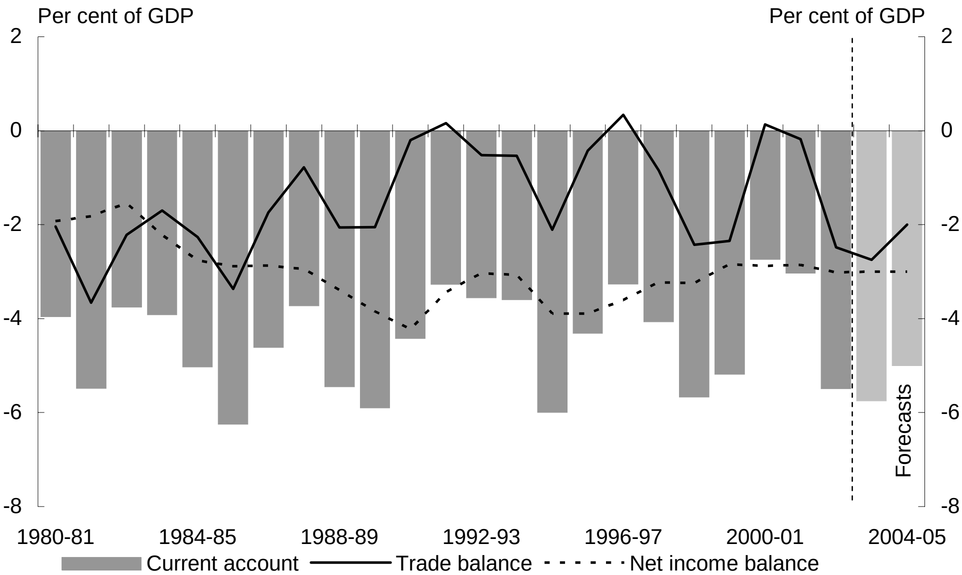
Strong growth in the terms of trade continues to provide an important buffer for Australian incomes, despite the relatively weak net export performance. This has contributed to the ability of the Australian economy to continue to grow through the period of downturn in the international economy.

The current account

The current account deficit is expected to narrow to 5 per cent of GDP in 2004-05, from the 5¾ per cent forecast for 2003-04 (Chart 10). As noted in last year's Budget, the widening of the current account deficit over 2002-03 and 2003-04 reflected the impact of the desynchronised Australian and world economic cycles and the drought. As the world economy recovers, the growth rate of GNE moderates, and rural exports recover, the current account deficit is expected to fall (Box 5).

Very strong growth in the terms of trade over recent years has cushioned the current account deficit from the full impact of the deterioration in net exports. Anticipated growth in the terms of trade drives the forecast narrowing of the current account deficit in 2004-05.

Chart 10: Current account balance



Source: ABS Cat. No. 5302.0 and 5206.0 and Treasury.

The net income deficit is forecast to widen in 2004-05, in line with the accumulation of net foreign liabilities associated with recent current account deficits, although it should remain relatively stable as a proportion of GDP. The net income deficit remains sensitive to the path of world interest rates. As the world economy recovers, there is a risk that rising world interest rates might increase the servicing cost on Australia's net foreign debt.

Box 5: The effects of desynchronised growth

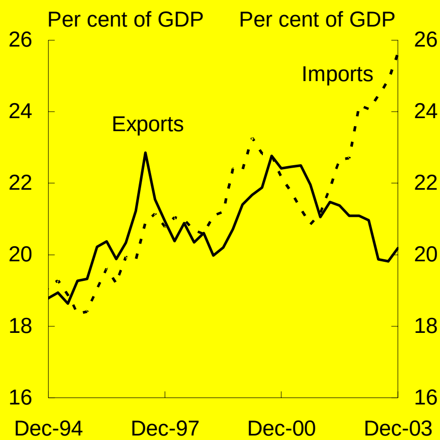
Import demand has been supported by strong growth in the domestic economy over the past two years. In contrast, Australia's exports have been subject to a series of supply and demand shocks. The weak world economy, the impact of 11 September 2001, the SARS outbreak and the collapse of Ansett Airlines have all constrained demand for Australian exports. The supply of exports was also affected by the severe drought in 2002.

The desynchronisation of growth between the domestic and world economies led to imports increasing faster as a share of GDP than exports (Chart A). Overall, net exports detracted more than 5 percentage points from GDP growth in 2002-03 and 2003-04.

As a trading economy, exports make up a relatively larger share of Australia's GDP than they do for some other developed countries. This makes the economy relatively more vulnerable to external shocks. Economic policy often has little or no ability to ameliorate the effects of these shocks when they occur. Therefore, it is important to focus beforehand on economic reforms that strengthen the economy and increase its flexibility to ride out shocks.

In recent years, reforms have been introduced to enhance competition in product markets and increase the flexibility of the labour market, the objectives of monetary and fiscal policy have been more clearly specified and the tax system has been overhauled. All of these reforms have contributed to making the economy stronger and more flexible. Nevertheless, it is important to continue to pursue economic reforms that facilitate trade and enhance Australia's ability to withstand future shocks.

Chart A: Exports and imports



Source: ABS Cat. No. 5206.0.

Labour market, wages and prices

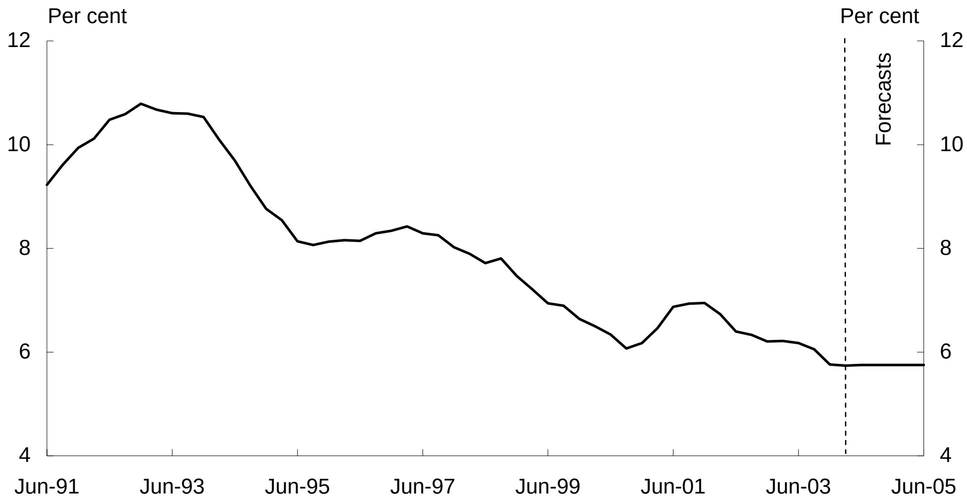
Labour market

Australia's unemployment rate is forecast to remain at, or close to, 23-year lows over 2004-05. For a detailed discussion of low unemployment in Australia, see Statement 4.

Growth in labour costs is expected to remain moderate, supporting the outlook for solid employment growth. This outlook is consistent with leading measures of labour market conditions. Job vacancies data remain at solid levels, with the ANZ job advertisements series being around its highest level in 10 months in March 2004. Surveys of business hiring intentions also point to solid employment growth in the near term.

Employment growth is expected to fall slightly to 1½ per cent through the year to the June quarter 2005, in line with a forecast decrease in through-the-year non-farm GDP growth. The forecast rate of employment growth should be sufficient to maintain the unemployment rate at around 5¾ per cent over 2004-05 (Chart 11), assuming that the participation rate remains around current levels.

Chart 11: Unemployment rate



Source: ABS Cat. No. 6202.0 and Treasury.

Over 2004-05, the composition of non-farm GDP growth is expected to be underpinned by growth in relatively capital intensive sectors of the economy, particularly mining. This presents a risk that employment growth might be slightly lower than would normally be the case for the forecast level of economic growth (see Box 6 for a discussion of the composition of employment growth).

Farm employment is expected to pick up through the forecast period, in line with the rebound in farm production. However, farm employment is likely to remain well below pre-drought levels until the livestock sector fully recovers over the next few years (see *Economic Roundup, Autumn 2004*, pages 25-42).

Box 6: Employment intensity and industry drivers of GDP growth

Industries in Australia differ markedly in terms of their labour intensity. For example, in 2003 the mining industry employed three workers per million dollars of gross value added (GVA) production, while the retail trade industry employed 37 workers per million dollars of GVA production (Chart A).

Chart A: Selected industry employment intensity[(a)]

(a) Persons per million dollars of GVA.
Source: ABS Cat. No. 5206.0, 6105.0.

In recent years, GDP growth has been driven by solid growth in industries that are both relatively intensive users of labour resources and significant employers; in particular, construction, property and business services and retail trade.

A rebalancing between the industry drivers of GDP growth is expected to occur in 2004-05. Growth is expected to moderate in a number of industries which are relatively more employment intensive, such as construction. In contrast, growth is expected to pick up in a number of industries that are relatively more capital intensive, such as mining and agriculture.

Overall employment growth is expected to remain solid, but a little below the rates recorded in recent years. The relatively capital-intensive nature of the industry composition of the forecast growth suggests that employment growth is likely to be weaker than might otherwise be expected, given forecast output growth.

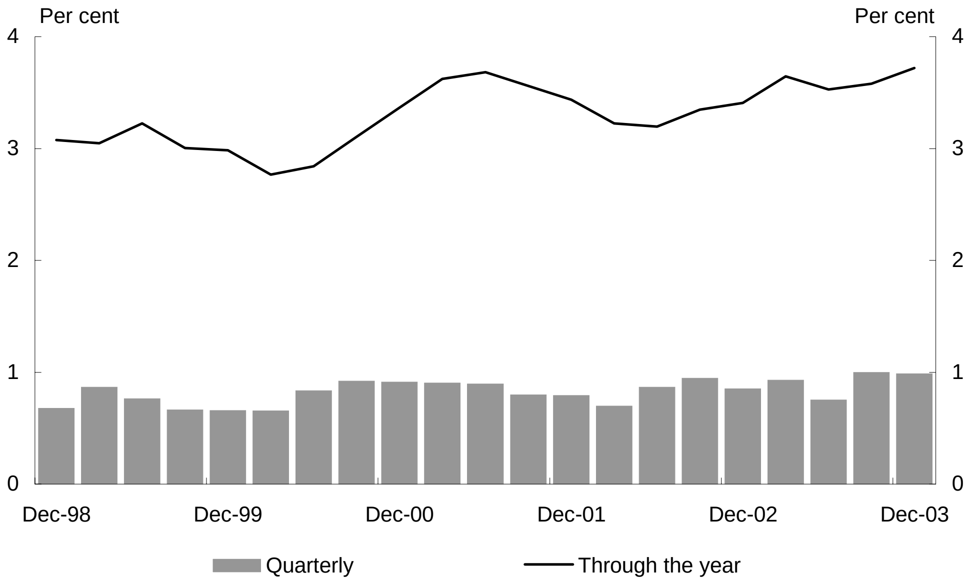
Wages

Growth in labour costs has remained moderate (Chart 12) despite the unemployment rate having fallen to near 23-year lows in recent months. Increased flexibility flowing from labour and product market reforms has helped to contain labour costs compared with previous episodes of low unemployment. Business liaison suggests that employers are having some success in finding productivity offsets to deal with localised wage pressures. The significant growth in part-time employment also provides an outlet for labour market pressures, with some part-time employees willing and able to take on more hours as the economy expands (see Statement 4 and *Economic Roundup*, *Autumn 2004*, pages 1-20 for a more detailed discussion of these issues).

There is some evidence of isolated labour market pressure, with business surveys indicating that some employers are finding it difficult to obtain skilled labour, most notably in the construction sector. Wage pressures have also been evident in parts of the public sector and these pressures are expected to continue into 2004-05. However, this has not translated into generalised wage pressure. The forecast convergence of employment growth to around that of the labour force is expected to reduce the risk that currently isolated wage pressures will spill over into more generalised wage demands.

Overall, wage pressures are expected to remain contained through 2004-05. Recent falls in the unemployment rate are forecast to lead to a slight firming in wage growth in the near term. However, the forecast moderation in non-farm GDP growth through the year to the June quarter 2005, and the associated slowing in employment growth, should see these pressures ease. The Wage Cost Index (WCI) is forecast to grow at 3¾ per cent in both 2003-04 and 2004-05.

Chart 12: Wage Cost Index



Source: ABS Cat. No. 6345.0.

Prices

Inflation is forecast to slow to 1¾ per cent through the year to the June quarter 2005, down from around 2½ per cent through the year to the June quarter 2004, and below the medium-term inflation target band.

Growth in the headline Consumer Price Index — the inflation measure targeted by the Reserve Bank of Australia — has fallen substantially over the past year, from nearly 3½ per cent in early 2003 to 2 per cent through the year to the March quarter 2004. Lower growth in tradables prices, largely reflecting the substantial appreciation of the

Australian dollar over the past year, has been a major contributor to these lower inflation outcomes (Box 7). Partly offsetting this, non-tradables prices have been increasingly driven by strong contributions from project home prices and the prices of health and education services.

The inflation outlook remains benign, with the past appreciation of the Australian dollar expected to continue to exert downward pressure on tradables prices for some time. Oil prices are assumed to increase over the near term given recent developments in the world oil market and then fall gradually over 2004-05, consistent with the oil price futures curve. In addition, tradables inflation will benefit from tariff reductions on motor vehicles and textiles, clothing and footwear from 1 January 2005. Food prices are also expected to moderate as the effect of the drought diminishes.

Capacity constraints are expected to ease a little over 2004-05, in line with forecast lower through-the-year growth in non-farm GDP and recent strong business investment. An assumed moderation in the growth rate of project home prices is also expected to contribute to an easing in non-tradables inflation.

Movements in labour costs remain an important determinant of inflation. With the unemployment rate forecast to hold steady through 2004-05 and wage growth forecast to remain moderate, there is little evidence of a strong impetus to inflation pressures from this source. Nevertheless, given high levels of capacity utilisation, the possibility that current isolated skill shortages and wage demands could widen into more generalised wage pressures presents a risk to the inflation forecasts.

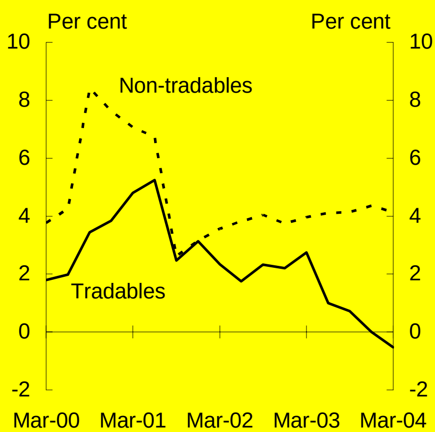
Box 7: The outlook for inflation

Inflation has fallen steadily over the past year, to be 2 per cent through the year to the March quarter 2004. However, the prices of tradable and non-tradable goods have followed divergent paths in recent years (Chart A).

Inflation of tradable goods and services has been falling, and has been negative in recent quarters, reflecting strong competitive pressures in the world economy and the higher exchange rate.

The exchange rate will continue to restrain increases in the prices of tradables since it takes some time for the effect of an exchange rate movement to pass fully through to retail prices.

Chart A: Inflation components



Source: ABS Cat. No. 6401.0.

Inflation of non-tradables, on the other hand, has increased to more than 4 per cent, reflecting price increases for project homes and some services such as health and education.

The forecast moderation in housing construction activity is expected to take some pressure off project home prices. The recovery of farm production from the drought should also lead to lower inflation for food items, although continuing dry conditions in parts of Australia may slow this effect.

Taking these factors together, the outlook is for inflation to remain low over 2004-05, despite the divergence between tradable and non-tradable prices.

While inflation of non-tradables is expected to fall as housing activity slows, inflation of tradables is likely to increase once the pass-through of the higher exchange rate is complete.

STATEMENT 4: MAINTAINING LOW UNEMPLOYMENT IN AUSTRALIA

Statement 1 outlines the need to take early action to increase productivity and labour force participation in order to boost Australia's medium-term growth potential and address the ageing of the population already underway.

The rise in unemployment in Australia, commencing in the 1970s, meant that the contribution of labour force participation to real growth in GDP per capita fell over the past 40 years.

Over recent years, Australia's unemployment has been on a steady downward trend. Now below 6 per cent, it is around 23 year lows and is expected to remain low over the forecast period. Unemployment sustained around these levels marks an important breakthrough against the poor unemployment outcomes recorded from the mid-1970s.

Policy reforms have helped to create the circumstances where unemployment has fallen steadily and sustainably. The labour market is now more flexible, and the economy is less prone to the boom–bust cycles of the past as a result of product market reforms and steadier macroeconomic policy settings.

Further reform is announced in the 2004-05 Budget, which puts in place a package of major initiatives that address directly the objective of increasing economic growth by increasing participation and productivity. The package will assist with reducing welfare traps for those receiving family tax benefits and deliver tax cuts that will increase the reward from working. The Budget also contains initiatives that increase investment in education, health, innovation and infrastructure that will assist participation and productivity.

These initiatives, together with the current solid macroeconomic environment, will enable Australia to achieve lower unemployment and higher labour force participation, provide a higher level of social wellbeing and help deal effectively and sustainably with the ageing of the population.

CONTENTS

MAINTAINING LOW UNEMPLOYMENT IN AUSTRALIA

INTRODUCTION

The unemployment rate is one of the most widely monitored partial indicators of a country's economic performance and the wellbeing of its society. Australia's unemployment rate has been sustained at around 23 year lows since late 2003, below 6 per cent, and there is scope for it to fall further over the medium term with appropriate policy settings.

Economic and social outcomes are enhanced when low unemployment is combined with high productivity in an environment where people can make sound decisions about participation in the labour force. This is evident in a number of ways. Average household incomes are likely to be higher and more stable than otherwise; income is likely to be more evenly distributed across the community, given that unemployment or non-participation in the labour force is a key contributor to relative poverty in the community; employed individuals and households tend to be more actively engaged in society and social activities; and a steady stream of income from regular employment provides individuals and households with greater opportunity to save, borrow and invest for their future and to contribute to the education of their children.

Unemployment sustained at around or below 6 per cent marks a major break from the past. Unemployment has averaged around 7½ per cent over the period since the late 1970s, but had only dipped to around 6 per cent briefly on two occasions prior to 2002. In the late 1980s, the decline in unemployment to around 6 per cent was accompanied by concerns about excessive strength in demand, a widening current account deficit and the prospect of rising inflationary pressure. A subsequent sharp slowdown in the economy saw unemployment rebounding to nearly 11 per cent over the next few years. In 2000, the decline to around 6 per cent saw only a modest push up in wage and price pressures, with unemployment rising to around 7 per cent for a short time as the economy slowed in line with weakening world growth and high oil prices, before resuming a downward trend.

The circumstances surrounding Australia's current economic performance are quite different to those earlier episodes and point to unemployment rates of 6 per cent or less now being much more sustainable. Economic and employment growth has been steadier, avoiding a build-up of inflationary pressure, as evidenced from a wide range of indicators such as wage costs, participation rates, hours worked, and a more even regional distribution of employment growth and falls in unemployment.

The improving performance of the labour market reflects a payoff from the wide range of macroeconomic and microeconomic reforms implemented over the last decade. Consistent macro policy settings, in a medium-term framework, since the mid-1990s are contributing to steadier economic and employment growth. Coupled with the increased flexibility of the economy flowing from the long-term programme of microeconomic reform, this is making the economy less prone to the booms and busts of the past, which made it difficult to achieve a steady and sustainable approach to low unemployment levels. Flexible workplace relations and active labour market programmes, along with increased participation in education and training, have contributed to a more flexible, adaptable and responsive labour market. Better incentives to participate in the labour force and for the unemployed to actively seek employment have come through reductions in income tax rates and reforms to income support arrangements.

Australia's current unemployment rate is not only low relative to the experience of recent decades, unemployment in Australia has been below the OECD average since late 2001, the first time it has been lower than the OECD average for a sustained period since the late 1980s. But there are several developed economies with unemployment rates below Australia's, for example New Zealand and Ireland. Structural unemployment rates in the United States also seem likely to be lower than in Australia. This suggests there is scope to sustainably lower unemployment further in Australia over the medium term, with ongoing steady growth and further policy reform.

The first section of the Statement reviews the performance of the labour market in recent decades with a focus on unemployment. An emphasis in this section is placed on a comparison of the circumstances surrounding the decline in unemployment to around 6 per cent in the late 1980s, 2000 and the most recent period since 2002. The second section of the Statement surveys the changes in policy settings which have contributed to the improved labour market performance in recent years and considers where there may be scope for policy settings to be tuned to further reduce unemployment.

TRENDS IN THE UNEMPLOYMENT RATE OVER RECENT DECADES

Unemployment in Australia since the Second World War

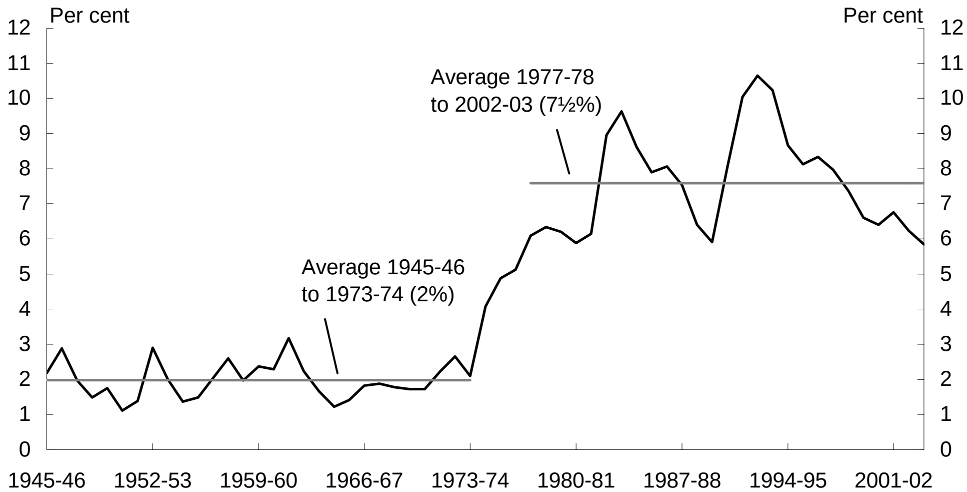
The unemployment rate is influenced by a range of factors. These include the prevailing economic environment, the institutional and policy framework for the labour market, and a range of social factors such as attitudes towards desired hours of work and willingness to move locations or undertake further training in order to secure employment.

Chart 1 illustrates Australia's measured unemployment rate over the period from the end of the Second World War to 2003-04 (Box 1 briefly reviews the trends in unemployment in Australia between Federation and the Second World War). It is evident from the chart that unemployment rates have traditionally been subject to significant short-term fluctuations. It is also evident that there was a substantial increase in the average unemployment rate from the mid to late 1970s, compared with earlier decades.

In the period from the Second World War to the mid-1970s, the unemployment rate fluctuated around a longer-term average of 2 per cent, reaching as high as around 3 per cent, with a low point of around 1 per cent. In contrast, in the period from the mid-1970s to the early 2000s, the unemployment rate fluctuated around a longer-term average of 7½ per cent, reaching as high as 10.9 per cent in 1992, with a low point currently below 6 per cent.

These longer-term average rates of unemployment are sometimes referred to as structural unemployment rates, on the assumption that they are more likely to reflect the longer-term economic, institutional and social factors driving the labour market. These factors can change over time, and when they change the structural rate of unemployment will change. However, most moves in the unemployment rate are not structural, but rather reflect only short run or cyclical swings in economic activity.

Chart 1: Australia's unemployment rate, 1945-46 to 2003-04

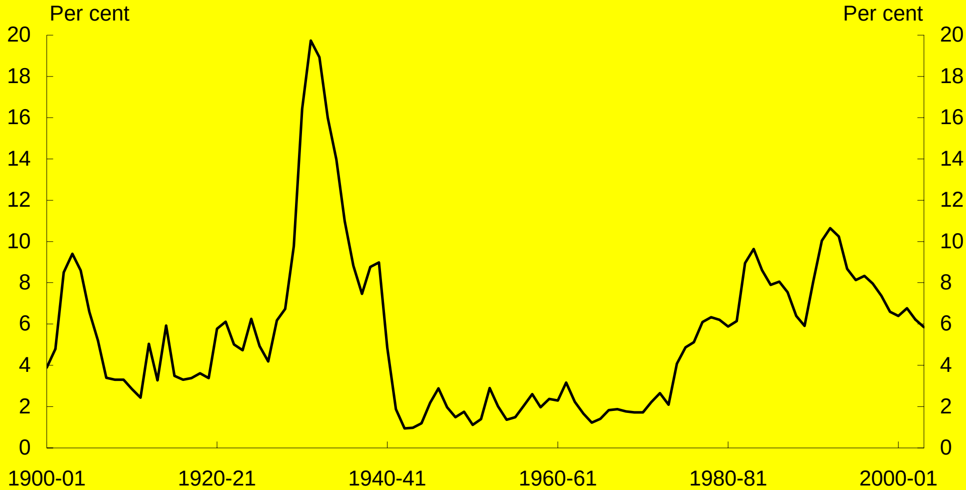


Source: Data to 1965-66 from *Preliminary Annual Database 1900-01 to 1973-74* (Reserve Bank of Australia Research Discussion Paper 7701). Data from 1966-67 to the present is from *Labour Force, Australia* (ABS Cat. No. 6202.0). 2003-04 figure is the average for the nine months to March 2004.

The increase in the structural rate of unemployment since the mid-1970s likely reflected a range of factors. In the 1970s, poor macroeconomic policy management (especially in the face of the first oil price shock), combined with rigid institutional arrangements in the labour market and strong union influence, resulted in much higher inflation and a sharp increase in real wages relative to underlying trends in productivity. The resultant real wage 'overhang' resulted in a reduction in employment opportunities and rising unemployment as businesses reacted to the increased cost of labour.

Box 1: Australia's unemployment rate since Federation

Chart 2: Unemployment rate, Australia, 1900-01 to 2003-04



Source: Data to 1973-74: *Preliminary Annual Database 1900-01 to 1973-74* (Reserve Bank of Australia Research Discussion Paper 7701). Data from 1974-75: *Labour Force, Australia* (ABS Cat. No. 6202.0). 2003-04 figure is the average for the nine months to March 2004.

Chart 2 shows the level and variability of Australia's unemployment rate since Federation.[1] Australia's unemployment rate prior to the Great Depression in the early 1930s generally varied in a range between 3 and 6 per cent. The Great Depression was associated with a very large increase in unemployment, rising from just over 4 per cent in 1926-27 to over 19 per cent in 1931-32.

It then took a further 9 years, and the outbreak of the Second World War in 1939, for the unemployment rate to return to under 4 per cent. During the war, the labour market was distorted by the demand for military personnel, and so called 'manpower planning' in many key sectors of the economy.

Through the late 1970s productivity growth also slowed, prolonging and intensifying the effect the real wage overhang had on the unemployment rate. The existing centralised wage fixing system meant that wages were generally tied to inflation, so the real wage overhang could not be quickly removed over time. The early 1970s also saw a range of reforms to the social welfare system specifically aimed at providing a more generous and comprehensive welfare safety net. However, a consequence of

1 Care should be taken in interpreting this chart. The definition of unemployment has changed over time, and the estimates prior to the Second World War are relatively unreliable.

some of these reforms is likely to have been a reduced incentive for some unemployed people to actively seek work.[2]

The pattern of a substantial increase in both unemployment and inflation (often referred to as 'stagflation') was seen in many countries during the period of the late 1970s, and Australia's experience was not unique. Although starting from a higher base, the average unemployment rate jumped by around 2 percentage points in the less regulated labour market of the United States, and by an average of over 4 percentage points in the larger European countries with more regulated labour markets. The increase in average unemployment rates in Australia was one of the largest at around 5 percentage points (comparing 1960-1973 with 1973-1990), with Australia moving from having one of the lowest unemployment rates in the world to a relatively high rate. Box 2 provides further detail on longer-term trends in unemployment and inflation for Australia and some other OECD countries.

Chart 1 also shows that, since the sharp increase in unemployment in the 1970s, previous episodes of low unemployment have generally not been sustainable. They were often associated with an overheating economy, with the unemployment rate rebounding to higher levels shortly after reaching historical lows. The factors which drove these rebounds in unemployment are complex and likely to have varied from episode to episode. In broad terms, emerging tightness in labour markets as the unemployment rate declined towards the lower point is likely to have put increased pressure on wages (especially in the early 1980s), at least in some industries and regions, particularly if output and employment had been increasing rapidly.

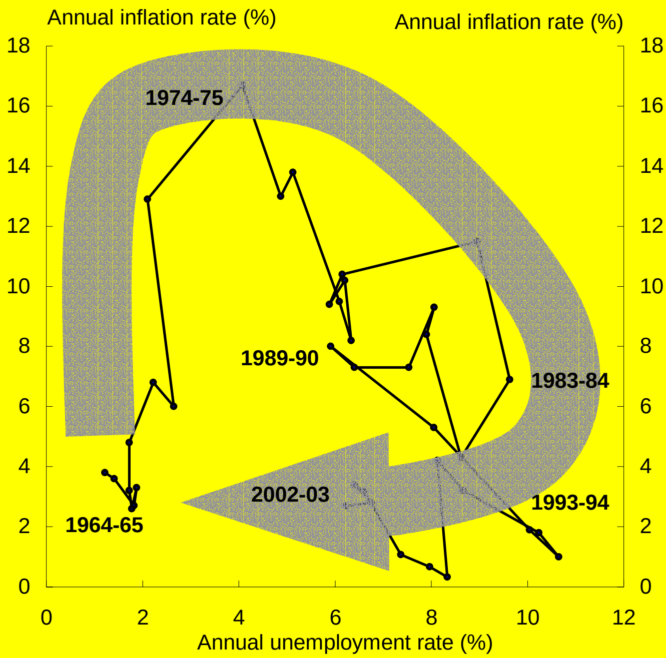
With centralised wage fixing, which Australia has had in some form over most of the period, wage pressures in one sector or region would quickly flow into other parts of the economy, even where labour demand pressures were less apparent. This, in turn, tended to raise concerns about increased inflationary pressure as higher wage costs were passed on in the form of higher prices, a process exacerbated by limited or restricted competition in the market for many goods and services. Put another way, whatever 'impulse' to the economy generated pressure for higher wages in one sector or region, the centralised wage system helped 'propagate' this to the broader economy. Limited competition in product markets then allowed this first-round inflationary effect to be embedded into the economy.

2 Further discussion of this structural increase can be found in J. Borland and S. Kennedy (1998), 'Dimensions, Structure and History of Australian Unemployment', in G. Debelle and J. Borland (eds), *Unemployment and the Australian Labour Market*, proceedings of a conference held by the Reserve Bank of Australia and the Australian National University, Sydney.

Box 2: Unemployment and inflation — the Phillips Curve

One way to measure the change in Australia's economic performance over time is to trace out the combination of inflation rates and unemployment rates recorded over a period of years. The result is sometimes referred to as a 'Phillips Curve'.[3]

Chart 3: The Australian Phillips Curve



Source: *Labour Force, Australia* (ABS Cat. No. 6202.0) and *Consumer Price Index, Australia* (ABS Cat. No. 6401.0), Treasury calculations.

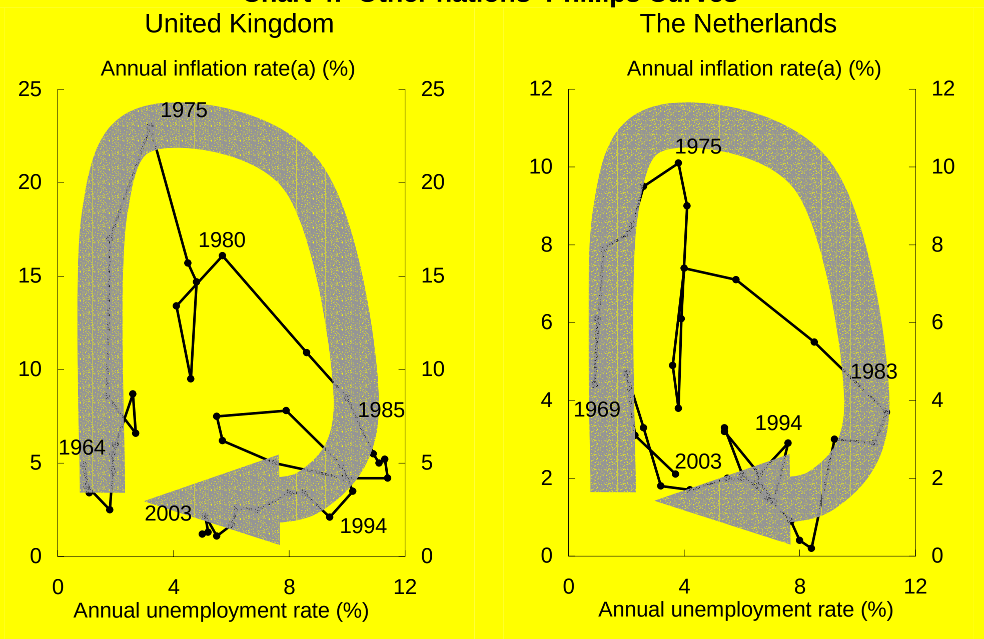
Australia recorded a combination of low inflation and low unemployment in the 1960s. In the 1970s, in response to poor macroeconomic policy settings and rising pressure for higher wages, inflation increased sharply and there was some increase in unemployment. Inflation moderated somewhat in the 1980s, but unemployment continued to rise on average. Since the early to mid-1990s, inflation has been sustained at much lower levels, and unemployment has been trending down. This more recent experience reflects the benefits of more stable and coherent macroeconomic policy settings and the impact of the longer-term programme of microeconomic reforms, which has made the economy much more adaptable and flexible.

3 Further discussion of the 'Phillips Curve' in Australia is contained in D. Gruen, A. Pagan and C. Thompson (1999), 'The Phillips Curve in Australia', *Journal of Monetary Economics* 44(2), pp. 223-258.

Box 2: Unemployment and inflation — the Phillips Curve (continued)

Chart 4 shows that the United Kingdom (UK) and the Netherlands' Phillips Curves over a similar time period display many of the features revealed in the Australian curve. Like Australia, both these countries undertook broad structural reform programmes during the 1980s and 1990s which have recently enabled their economies to simultaneously demonstrate low inflation and moderately low unemployment rates.

Chart 4: Other nations' Phillips Curves



(a) Private consumption deflator growth rate.
Source: OECD Economic Outlook database.

Governments and monetary authorities tended to respond to these inflationary pressures by tightening fiscal and monetary policy (either through 'credit rationing' in earlier periods when financial markets were highly regulated, or higher interest rates in more recent decades) to slow the economy and reduce inflationary pressure, thereby exacerbating (or magnifying) the negative consequences for employment of the original shock.

Once inflationary pressures had emerged, it often required a period of much slower economic and employment growth, and hence a sustained period of higher unemployment, to reverse the process, particularly in the absence of a coherent and credible medium-term macroeconomic strategy and framework in earlier decades, and the absence of flexible labour markets. Further, it usually proved difficult for policy makers to judge the required extent of tightening of fiscal and monetary policy to quell the emerging inflationary pressure.

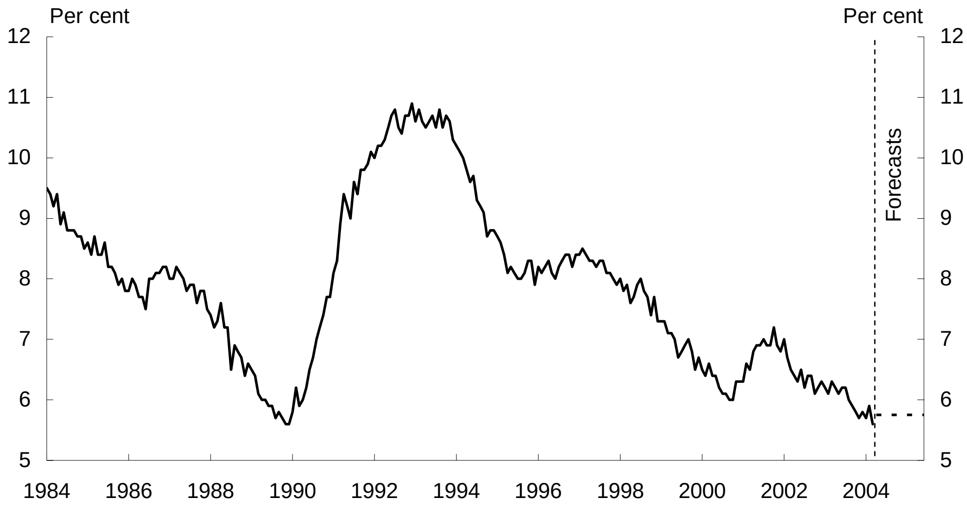
This created the risk that either too little would be done initially and inflationary pressure would continue to build, followed by an excessive tightening of policy and a very sharp slowdown in growth and rise in unemployment, or policy would be tightened excessively in the initial response.

As discussed in more detail in the next section, Australia's unemployment experience since 2002 stands in contrast with these earlier outcomes. Unemployment has declined steadily to below 6 per cent and is expected to remain below 6 per cent on average over the forecast horizon, in the context of steady economic growth and minimal wage and price pressures.

The labour market in the 1980s, 1990s and 2000s

Chart 5 shows Australia's unemployment rate for the past 20 years in more detail, including the Budget forecasts out to mid-2005. Following the structural upward shift in the unemployment rate in the late 1970s Australia's unemployment rate has declined to levels around 6 per cent on only three occasions: 1989 to 1990, late 2000, and late 2002 to the present.

Chart 5: Unemployment rate, Australia, 1984 to 2005



Source: *Labour Force, Australia* (ABS Cat. No. 6202.0), Treasury forecasts.

These three episodes have had quite different aftermaths. In the case of the 1989 episode, the unemployment rate subsequently rose sharply, reaching almost 11 per cent by 1992. Following the 2000 episode the unemployment rate rebounded modestly, but only to slightly over 7 per cent, before resuming a downward trend. In contrast, in the current episode, the unemployment rate has been around 6 per cent for an extended period since October 2002, and has been below 6 per cent since September 2003. The unemployment rate is expected to remain below 6 per cent on average over the forecast horizon. Statement 3 in this Budget Paper contains more detail about the forecasts for the labour market.

While the unemployment rate declined to around 6 per cent in each case, there are significant differences in the overall performance of the labour market in the three periods, particularly with respect to employment growth, wage pressures, hours worked and regional variability in unemployment. As discussed below, these various indicators point to the current decline in unemployment to below 6 per cent being much more sustainable than previously.

Employment growth

In the 1989 episode the overall annual rate of employment growth was very high, at around 4 per cent. In fact, the through-the-year growth of 5 per cent experienced in the year to May 1989 has only been exceeded during one three-month period (in 1986) since monthly data collection commenced in 1978. This period of strong growth in employment was largely a reflection of very strong growth in output. The economy grew by around 5½ per cent in the year to the September quarter 1989 (when some of the lowest rates of unemployment for the episode were reached).

The period between May 1989 and November 1989 includes four of the ten highest through-the-year growth rates in total employment on record. Between June 1988 and April 1989, when the unemployment rate declined from over 7 per cent to 6 per cent, employment grew at an annualised rate of 4½ per cent.

In comparison, between September 1999 and September 2000, when the unemployment rate declined from 7 per cent to 6 per cent, employment growth was steadier but still above trend at just over 3 per cent (in annualised terms). The more subdued employment growth reflected the overall growth of the economy, which reached 4 per cent through-the-year to the June quarter 2000, and was 3½ per cent through-the-year to the September quarter.

During the most recent episode, the unemployment rate declined from 7 per cent in January 2002 to 6 per cent in August 2003. During that period, employment grew at an annualised rate of 2 per cent, broadly in line with the longer-term average growth rate of employment in Australia. Growth in the overall economy was also relatively steady, at 2.7 per cent through-the-year to September 2003 (although this growth rate was below trend due to the continued impact of drought on the agricultural sector and the global slowdown).

The annual growth rate of employment did reach 3 per cent briefly in this period, but returned to trend rates soon after. Employment growth has been maintained at around trend rates since then as the unemployment rate has trended down further to below

6 per cent in recent months. These sustainable rates of employment growth have helped to contain wage and price pressures as the unemployment rate has declined.

The steadier and more stable growth in employment in the two most recent episodes reflects the more stable growth in overall GDP.[4] And this in turn reflects the improvements to overall macroeconomic policy frameworks, and the long-term programme of microeconomic reform, which have helped to provide greater stability to the overall economy. These issues are discussed in more detail in the second section of this paper.

Other indicators of labour market tightness

While the unemployment rate is the most commonly used summary measure of the state of the labour market, it does not capture the full story of what is happening within the market. Movements in the unemployment rate are, in fact, the result of large flows into and out of employment, and into and out of the labour force, and the unemployment rate captures only the net impact of these flows (Box 3). Over time these flows will also have an impact on the industry distribution of employment (see Box 4).

Movements in other labour market indicators, discussed below, can also provide useful additional information about the possible emergence of excessive tightness or imbalances in the labour market, and hence how sustainable the unemployment rate may be over the medium term.

Growth in labour costs

One such indicator to assess the relative tightness of the labour market, and hence the sustainability of the unemployment rate, is the trend in the growth rate of labour costs. A very tight labour market is likely to be associated with accelerating wages growth relative to growth in productivity and hence rising labour costs. One measure which captures such changes in wage growth relative to productivity trends is Nominal Unit Labour Costs (NULCs).[5]

Chart 6 shows that NULCs grew by nearly 8 per cent in the year to the March quarter 1989. The average growth rate of NULCs was above 7 per cent for 7 of the 8 quarters between December 1988 and September 1990, which is the longest period above 7 per cent since the early 1980s (when NULCs growth reached as high as 18 per cent in 1982). This reflected both relatively high growth in wages, but also very poor growth in productivity, with labour productivity actually falling by 1½ per cent in the year to the March quarter 1990.

---

4 See Budget Paper No. 1, *Budget Strategy and Outlook 2002-03*, Statement 4, pp. 4-10 to 4-11.

5 Real Unit Labour Costs can also be used to assess changes in labour costs taking into account the effects of inflation, although the trends are broadly similar to those for NULCs.

Box 3: The dynamics of the labour market

An increase in unemployment is often considered to be a reflection simply of a loss of jobs, while a decrease in unemployment is interpreted simply as people finding jobs. However, the reality of the labour force is that jobs are both lost and gained in large numbers during any given month. There are also people moving in and out of the labour force, as well as growth in the potential labour force as the population increases. These movements in and out of employment and the labour force can occur for a variety of reasons, of which losing a job is only one. Other examples include people taking the opportunity for a holiday between contracts, occupations where employment is seasonal, or leaving the labour force to care for children.

During 2003 the number of unemployed persons in Australia fell from a seasonally adjusted level of 632,000 in January 2003 to 584,000 by the end of the year. Taken simply, this suggests that 50,000 people moved from unemployment to work. But breaking down these figures shows that in fact, in every month around 130,000 people move from unemployment to work, and around 92,000 move from employment to unemployment. All together there were 1.6 million movements from unemployment to work (either part-time or full-time), and 1.1 million movements from work to unemployment. The final change in unemployment further depends on flows between unemployment and those not in the labour force, and the growth in the population aged over 15.

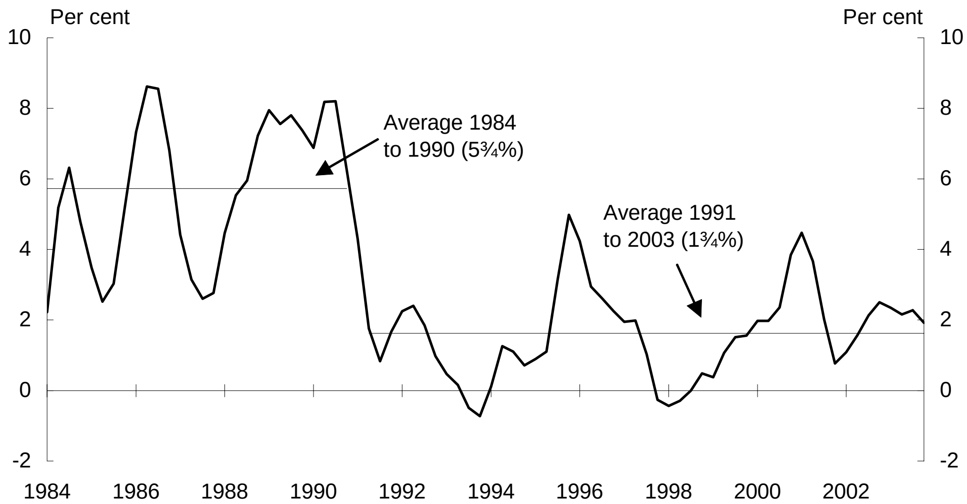
It is clear that it is these flows, and the factors behind them, that are the most important force in determining the unemployment rate. In particular, small changes to these flows can have large impacts on the overall movement in the measured unemployment rate. Small disincentives to work or create jobs can have large consequences, as over time even small differences in flows can be reflected in large numbers of people being recorded as unemployed at given points in time.

While around 50 per cent of those currently unemployed were unemployed for less than 3 months in 2003, there was a significant group who had been unemployed for longer, with a fifth of people unemployed having been so for a year or more. So while these flows show that there are people constantly moving in and out of unemployment, there is also a group of long-term unemployed for whom re-entry into employment can be particularly difficult.

In contrast, the episode in 2000 saw a more modest increase in labour costs, and the period since 2002 has seen minimal pressure on labour costs to date. Between June 2000 and March 2001 NULCs growth increased from 2 per cent to 4½ per cent. However, part of this acceleration was a return to more normal rates of growth, from the low and even negative rates experienced in 1998 through early 2000. Productivity growth also slowed somewhat, from the relatively high annual rates of 3 to 4 per cent through the late 1990s to an average annual growth rate of less than 1 per cent through 2000.

In 2002 and 2003 growth in NULCs was very modest at around 2 per cent per annum, only slightly above the average for the 1990s, and trending downwards slightly in recent quarters. This is indicative of the combination of steady employment growth, a gradual downward movement in unemployment and a more flexible labour market helping to prevent excessive tightness in the labour market and the associated increases in labour costs. Another contributing factor was a strong productivity performance, with through-the-year growth rates averaging around 2 per cent over 2002 and 2003.

Chart 6: Growth in nominal unit labour costs (through-the-year), 1984 to 2003



Source: *Unit Labour Costs*, Australian Government Treasury.

The lower and more stable growth in unit labour costs over recent years is another dividend from the improvement to the macroeconomic framework and labour markets, especially the lower inflation rates that have been sustained over the last decade or so compared to the inflation rates in the 1980s. Lower inflation, and lower inflation expectations, improves the wage bargaining process as both employers and employees can be more certain of the future path of prices.

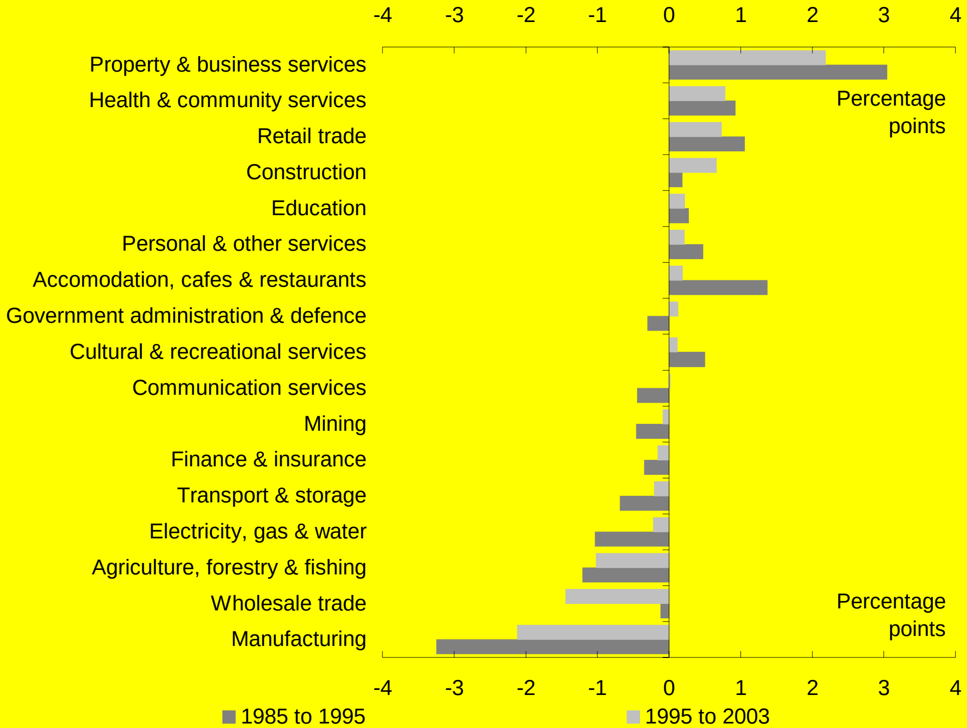
Participation rates

Another indicator of emerging labour market tightness is rapid increases in the participation rate in the short term. The participation rate measures how many people in the working age population (defined in Australia as those 15 years of age or older) are looking for or have a job. When the participation rate rises rapidly in the short term, in the context of strong employment growth, it often indicates that the labour market is tightening.

Box 4: Industry distributions of employment

A decline in employment in one industry or sector, in relative or absolute terms, does not necessarily represent a decline in employment for the economy as a whole. In a flexible, adaptable economy, lower employment in one sector is generally offset by increasing employment in other sectors.

Chart 7: Change in share of total employment by industry



Source: *Labour Force, Australia, Detailed* (ABS Cat. No. 6291.0.55.001).

Chart 7 shows how the industry by industry shares of total employment have changed over the past 18 years. Some industries that have traditionally been large in Australia have declined relatively, such as manufacturing. And in their place employment has grown more strongly in the services sector.

One important note on these shifts is that they occur within the context of a growing labour market — between 1985 and 2003 the total level of employment grew by over 40 per cent. Most of the declines shown in Chart 7 are purely relative declines, and do not reflect levels of employment, only that the industry is not growing as fast as others. For example, while the share of total employment in wholesale trade has fallen by 1.6 percentage points between 1985 and 2003, total employment in that sector has grown by around 22,000 jobs over the same period.

When the unemployment rate fell from 7 per cent to 6 per cent in 1989, the participation rate rose by around ½ of a percentage point. The episode in 2000 saw a similar increase in the participation rate over the period where the unemployment rate fell from 7 per cent to 6 per cent. But this fall in unemployment occurred over a longer period, suggesting that there may have been less tightness in the labour market.

In contrast, when the same decline in unemployment occurred in 2002 the participation rate was lower at the end of the period (although it did fluctuate upwards for 6 of the 18 months in question). This is partly a result of a steadier approach to low unemployment levels than in previous episodes.

The longer-term trends in Australia's participation rates are largely driven by structural factors, rather than short-term labour market fluctuations. The most significant driver of the Australian participation rate over the past four decades or so has been the increasing participation of women in the labour force. Looking forward, participation rates will be strongly influenced by the ageing of the population, as discussed in the *Intergenerational Report* contained in the 2002-03 Budget Papers. [6]

Other important structural factors include the incentive that individuals on welfare and other benefits have to enter employment, the education and skills attainment of those entering the labour force, and the options for retraining and further education available to those who have become unemployed. The influence of these factors is discussed in more detail later in this paper.

Part-time employment

Another dimension to the issue of possible increasing tightness in the labour market, and hence the sustainability of the unemployment rate, is the impact of part-time work. The growing importance of part-time work reflects a significant structural change in the labour market in Australia. Australia has one of the highest rates of part-time work in the world, reflecting a relatively flexible labour market that allows many people to choose the number of hours of work that best suits their individual circumstances.

Since the mid-1960s the proportion of employees working part-time (that is, working less than 35 hours per week) has grown from around 9 per cent to around 30 per cent today. This increase reflects a long-term improvement in the ability of people to choose how they will participate in the labour force, and how many hours they will work.

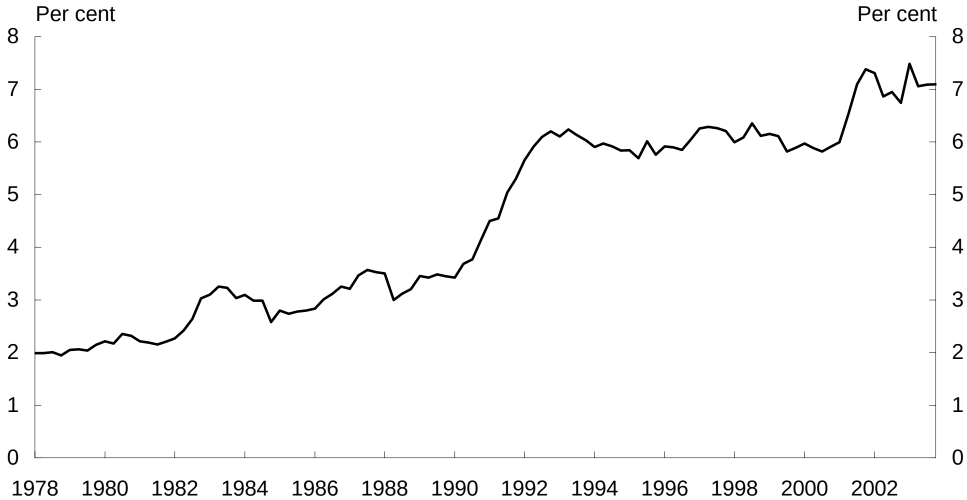
Survey data indicate that around three quarters of part-time workers are not actively seeking more hours. The fact that the majority of part-time workers are satisfied with their existing hours of work is testament to the flexibility of Australia's labour market, and its ability to deliver employment arrangements which are satisfactory for both employees and employers. Nevertheless, there is still a pool of part-time workers who

---

6 Australian Government (2002), Budget Paper No. 5, *Intergenerational Report 2002-03.*

would work more hours if such employment opportunities became available (about one quarter of part-time workers, and hence around 7 per cent of the total labour force). This could provide an additional 'buffer' against emerging wage and price pressures when there is rapid growth in employment.

Chart 8: Proportion of labour force working part-time and available for more hours of work, 1978-2003



Source: Treasury calculations based on *Labour Force, Australia* (ABS Cat. No. 6202.0) and *Underemployed Workers, Australia* (ABS Cat. No. 6265.0).

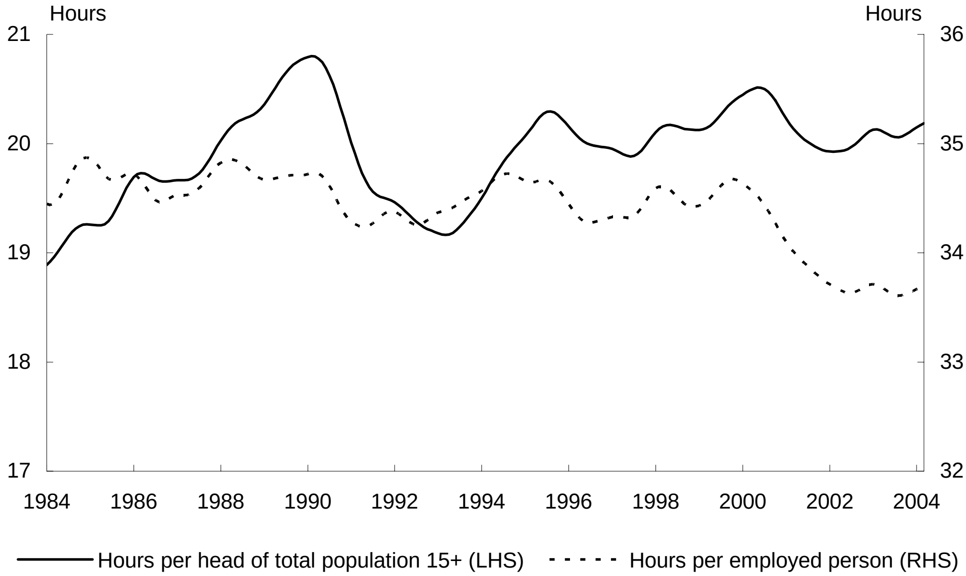
Chart 8 shows that the proportion of the total workforce that wish to work more hours has grown over the past 20 years, but is a comparatively small proportion of the workforce.

Average hours worked

Chart 9 shows an alternative summary indicator of the overall level of tightness in the labour market, namely the average number of hours worked per week per person aged over 15 (including those not employed or not in the labour force). This measure captures the net effect of not just the unemployment rate per se, but also employment growth, the participation rate, average hours of work for both full-time and part-time employees, and the relative proportions of full-time and part-time employment. Although the series is much more volatile than the unemployment rate, the overall trends are similar to the unemployment rate (Chart 5). In particular, on this measure, there are peaks of greater than average tightness in the labour market in 1989 and 2000. In contrast, there is less evidence of tightness in the current episode of low unemployment, with the hours measure peaking at a lower level than in the earlier episodes and subsequently trending down.

Chart 9 also shows the movements in average hours per employed person. The broad trends are similar, although the peaks in 1989 and 2000 are more moderate relative to trend than in the overall population. During these peaks, the additional demand for labour was met more by additional employment than changes in the hours worked by existing employees.

Chart 9: Average hours worked, Australia



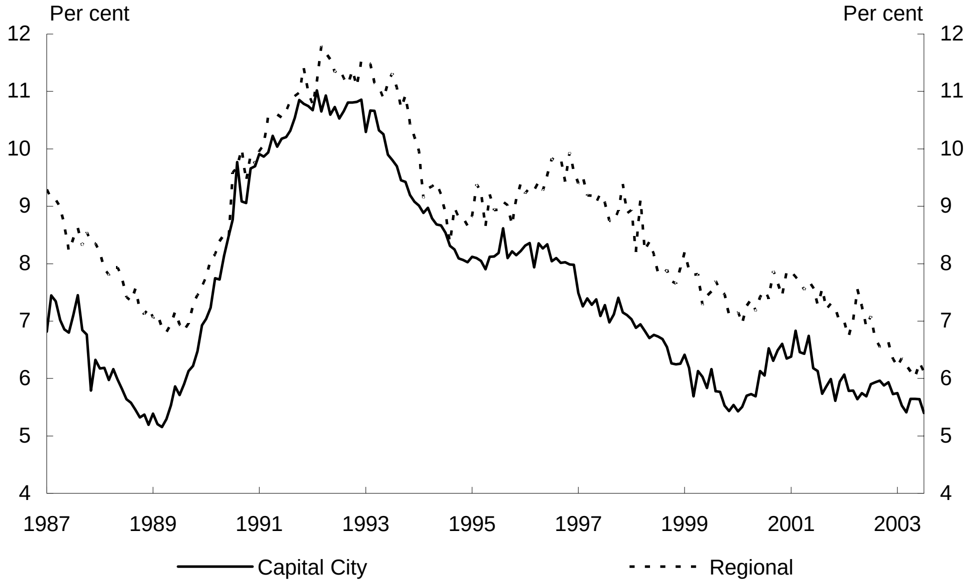
Source: Treasury calculations based on *Labour Force, Australia* (ABS Cat. No. 6202.0).

Regional unemployment rates

Labour market trends in particular capital cities might not reflect the labour market experience in other capitals or in more regional areas. For example, a period of labour market tightness, as measured by some of the overall national indicators, might reflect a very low unemployment rate in a few areas, such as Sydney and Melbourne, and higher unemployment elsewhere. In contrast, when the falls in the national unemployment rate reflect a relatively uniform fall in unemployment across most regions, there is less risk of bottlenecks and the associated price and wage pressures in particular areas or markets.

Historically, the capital cities have had a lower unemployment rate than regional areas. Chart 10 shows how these two unemployment rates have varied over the past decade and a half. The falling unemployment rate in 1989 and 2000 was relatively uniform across these two groups, and hence the gap between capital city and regional unemployment rates remained constant in both of these episodes. In contrast, during the most recent episode the most significant falls in unemployment have occurred in regional areas (notwithstanding the impact of the drought on farm employment), which has resulted in a closing gap between the capital city and regional areas. While unemployment rates in capital cities are currently somewhat above the lows of around 5¼ per cent reached in 1989, regional unemployment rates of just above 6 per cent are well below the rates of around 7 per cent reached in 1989 and 2000.

Chart 10: Unemployment rates for capital city and regional areas, 1987-2004



Source: Treasury calculations based on *Labour Force, Australia, Detailed — Electronic Delivery* (ABS Cat. No. 6291.0.55.001). Capital cities includes all State and Territory capitals except for Darwin, Regional includes the balance of Australia.

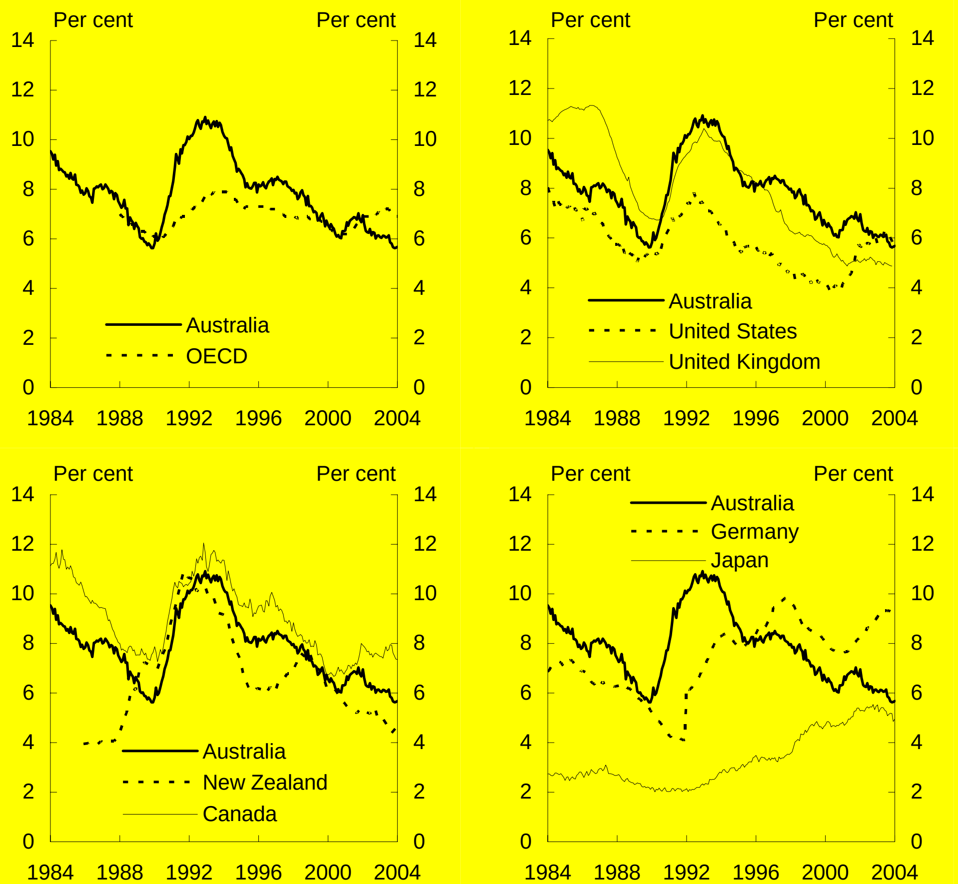
International trends in unemployment rates

Australia's current unemployment rate is not only low relative to the experience of recent decades, but also well below many other members of the OECD. The Euro area had an average unemployment rate of 8.8 per cent in 2003, with countries such as France and Germany experiencing unemployment rates above 9 per cent. Australia's unemployment rate is currently over 1 percentage point below the OECD average (in standardised terms), and has been below the OECD average since late 2001. This is a significant turn around since the mid-1990s, when Australia's unemployment rate was as much as 3 percentage points above the OECD average. Box 5 provides further detail on movements in unemployment rates in other key economies over recent decades.

That said, there are some countries with lower current unemployment rates than in Australia, such as New Zealand (averaging 4.7 per cent in 2003) and Ireland (averaging 4.6 per cent in 2003). The unemployment rate in the United States in 2003 was comparable to Australia, at around 6 per cent. However, this probably represented a cyclical peak for the unemployment rate in the United States reflecting the weak United States economy, while as discussed above, it represented a 23 year low in Australia. This suggests that the longer term or structural unemployment rates in the United States may still be below those for Australia.

Box 5: International trends in unemployment rates

Chart 11: Standardised unemployment rates in selected countries



Source: *OECD Main Economic Indicators*.

The extent to which unemployment rates fell in the 1990s differed across countries. While the UK unemployment rate fell from over 10 per cent in 1992 to less than 5 per cent in 2003, the German unemployment rate has stayed between 7 and 10 per cent since January 1993. Moreover, the long-term unemployed account for as much as one third of the total unemployed in Germany, reflecting structural problems in the German labour market.

Japan has been an exception to the general trend of falling unemployment rates during the 1990s. Prolonged weaknesses in aggregate demand has resulted in a doubling of Japan's unemployment rate from the 1980s average of 2½ per cent to the current 5 per cent.

Box 5: International trends in unemployment rates (continued)

A low unemployment rate may not always present a true picture of the labour market. While the rise in the US unemployment rate during the recent downturn has been modest by historic standards, the US labour market has weakened significantly, shedding 1.95 million jobs since March 2001 with the participation rate falling markedly. Similarly, the sustained fall in the Dutch unemployment rate during the 1980s and the 1990s happened in conjunction with a falling participation rate, which suggests that there may have been an increase in the number of 'discouraged' workers.

More generally, the fact that unemployment rates are lower in some other developed economies than in Australia suggests that there is scope to lower unemployment further in Australia over the medium term, given appropriate policy settings. This is discussed in more detail in the following section.

THE CONTRIBUTION OF POLICY REFORMS TO IMPROVED LABOUR MARKET PERFORMANCE

The first section of the Statement discussed how Australia's labour market performance has improved over time. Particular attention was drawn to the experience of the late 1980s, 2000, and the period since 2002. While the unemployment rate was around the low points of recent decades in each case, at around 6 per cent, the most recent period has been characterised by a structurally more sound economy, with steadier employment growth and low inflationary pressure. This suggests that low unemployment is now more sustainable and raises the prospect that unemployment can fall further.

The improved performance of the economy over recent years, of which the lower unemployment rate is an important dimension, has been achieved through a long-term and comprehensive package of reform measures. These measures have been complementary and reinforcing, and have been aimed at improving the microeconomic efficiency of the economy, its ability to grow steadily and consistently and to respond to change. An important characteristic of the reforms has been to ensure that the institutions affecting our social and economic activities are better suited to meeting contemporary and future needs.

The reforms have been extremely diverse and broad based, including: trade reform; deregulation of financial markets; wide-ranging tax reform; enhancing competition across many areas of the economy; increasing the flexibility of the labour market; the development of skills and capacities; reforms to welfare arrangements; and creating a transparent medium-term framework for fiscal and monetary policy in order to enhance economic stability. But there is scope to do more in some of these areas, to produce further gains in productivity, labour force participation, employment and overall wellbeing.

Lower unemployment brings valuable economic and social benefits. Higher income levels and a more equal distribution of income lower household poverty. Better access to income-earning activities provides greater opportunities for people to engage in economic and social activities, thus allowing the development of social capital. As a result of a more inclusive and connected society, with a greater capacity to support those who are disadvantaged, the risks faced by an individual in the modern economy are reduced. It is for these reasons that policies have been developed and refined in a balanced way to promote lower unemployment.

Policies to reduce unemployment from its current levels are needed to address the medium-term challenges which the Australian economy faces as a result of demographic change. In the 2002-03 Budget, the Government published the first *Intergenerational Report* in which it outlined the scale of these challenges, such as the effects on the potential labour force and living standards. In February 2004, the Treasurer released a discussion paper, *Australia's Demographic Challenges,* to promote community debate on these longer-term issues.[7]

In this context, this section surveys the changes in policy settings which have contributed to the improved labour market performance in recent years and considers where there may be scope for policy settings to be tuned to further reduce unemployment, including by removing the impediments to job creation and participation.

A framework for policy

The OECD has undertaken extensive cross-country research into the factors that drive employment and economic growth, culminating in the OECD Jobs Strategy[8] (see Box 6) and the related OECD Growth Study.[9] These strategies were in part developed in response to the stubbornly high rates of unemployment that many OECD nations have had since the 1970s.

The major elements of the OECD Jobs Strategy are to: increase the flexibility of working time and labour costs; reform employment security provisions; deliver active and effective labour market programmes; improve skills and competencies; and reform unemployment and related benefit systems and their interaction with the tax system.

---

7 Australian Government (2004), *Australia's Demographic Challenges*, February (http://demographics.treasury.gov.au).

8 OECD (1994), *The OECD Jobs Strategy*, Paris.

9 OECD (2003a), *The Policy Agenda for Growth*, Paris; OECD (2003b), *The Sources of Economic Growth in OECD Countries*, Paris.

The major elements of the overarching OECD Growth Study relate to: strengthening economic and social fundamentals; facilitating the diffusion of information and communications technologies; fostering innovation; investing in human capital; and stimulating the creation of firms.

Importantly, these strategies are complementary and need to be implemented together to have greatest effect on labour market performance. For example, reforms to welfare policies will not be as effective in improving employment and community wellbeing in the absence of steady macroeconomic management.

The elements of the OECD Jobs Strategy can be classified into three broad groups: general economic policies, labour polices and welfare policies. This provides a useful framework in which to survey the policy settings in Australia and how those settings have changed over time to address unemployment more effectively.

Recent policy reforms and areas for further development

Australian governments have made substantial progress in their general economic policies, labour and welfare policies over past years to achieve lower unemployment, consistent with the directions of the OECD Jobs and Growth strategies.

General economic policies

Critical to achieving low unemployment are: stable and well-tuned macroeconomic policies; well-functioning and competitive markets; innovation and a climate of entrepreneurialism; and the diffusion of new technologies. Policy developments in these areas and their contributions to wellbeing have been extensively discussed in previous budget papers.[10]

Since the 1970s, many reforms have been designed to improve the competitiveness of the Australian economy domestically and internationally. Greater competition and depth in Australia's product and financial markets has been fostered through mechanisms such as National Competition Policy, an agenda agreed by the Australian Government and State governments in the mid-1990s. Reforms have been implemented in the communications, energy and transport sectors, and by commercialising and privatising government businesses, removing anti-competitive regulation and broadening the scope of competition. Similarly, the reduction of barriers to trade and reduced support for export activity has opened the Australian economy to international competition, markets and cultures.

---

10 For example, Australian Government (2003), 'Sustaining Growth in Australia's Living Standards', Budget Paper No. 1, *Budget Strategy and Outlook 2003-04*, Statement 4.

Box 6: Summary of the OECD Jobs Strategy[11]

1. Set macroeconomic policy such that it will both encourage growth and, in conjunction with good structural policies, make it sustainable, that is, non-inflationary.

2. Enhance the creation and diffusion of technological know-how by improving frameworks for its development.

3. Increase flexibility of working time (both short-term and lifetime) voluntarily sought by workers and employers.

4. Nurture an entrepreneurial climate by eliminating impediments to, and restrictions on, the creation and expansion of enterprises.

5. Make wage and labour costs more flexible by removing restrictions that prevent wages from reflecting local conditions and individual skill levels, in particular of younger workers.

6. Reform employment security provisions that inhibit the expansion of employment in the private sector.

7. Strengthen the emphasis on active labour market policies and reinforce their effectiveness.

8. Improve labour force skills and competencies through wide-ranging changes in education and training systems.

9. Reform unemployment and related benefit systems — and their interactions with the tax system — such that societies' fundamental equity goals are achieved in ways that impinge far less on the efficient functioning of the labour markets.

10. Enhance product market competition so as to reduce monopolistic tendencies and weaken insider-outsider mechanisms while also contributing to a more innovative and dynamic economy.

11 J. Elmeskov (2000), *Implementing the OECD Jobs Strategy – assessing performance and policy*, remarks at the Conference on Jobs, Helsinki, January.

These improvements in competitiveness, combined with more strategic support by government for education, research and development, have gradually infused the economy with greater innovative capacities. Improvements in governance frameworks and corporate law have also played their role by ensuring transparency in economic activity, thereby enhancing the underlying confidence in the economy.

While many gains have been made under Competition Policy in a wide range of industries so far, there is scope to achieve further gains in efficiency, quality and resilience of the major infrastructure industries that provide critical inputs into many other economic sectors. Australian and State governments are looking to identify areas of opportunity for significant gain to be made through further competition reform, and the recently announced Productivity Commission inquiry is important in this regard.

The microeconomic foundations of the Australian economy are important to promoting lower unemployment. However, it is also worth highlighting the role that macroeconomic management plays in reducing unemployment. A medium-term framework for monetary and fiscal policies has been found to best contribute to steady and sustainable economic growth, helping to minimise the episodes of boom and bust due to poor macroeconomic policy that were a feature of Australia's past economic performance.

After the recession of the early 1990s Australian monetary policy started to focus around a medium-term inflation-targeting regime. In August 1996 in a *Statement on the Conduct of Monetary Policy* (the 'Statement') by the Treasurer and the Reserve Bank Governor a formal targeting regime was put in place and set out a target of 2 to 3 per cent on average over the course of the economic cycle. This Statement was reaffirmed and updated for current practice in July 2003. The Statement formalises the operational independence of the Reserve Bank in implementing monetary policy to achieve the Government's inflation goal. The inflation target provides discipline for monetary policy decision-making and serves as an anchor for inflation expectations in the community.

Australian fiscal policy was also placed by the Government into a medium-term framework from 1996. The *Charter of Budget Honesty Act 1998* (the 'Charter') states that fiscal policy should be directed at maintaining the ongoing economic prosperity and welfare of the people of Australia, and therefore should be set in a sustainable medium-term framework. The purpose of the Charter is to improve fiscal policy outcomes. It provides for this by requiring that fiscal strategy be based on principles of sound fiscal management and by facilitating public scrutiny of fiscal policy and performance. This transparency is important for the credibility of fiscal policy. The primary objective of the Government's fiscal strategy is to maintain budget balance, on average, over the course of the economic cycle.

A continuation of general microeconomic reform and sound macroeconomic policy settings will be important for assisting labour and welfare policies to maintain low levels of unemployment and to achieve further reductions in unemployment.

Labour policies

The first section of this Statement indicated that Australia's unemployment rate has averaged 7½ per cent since the late 1970s. A belief that lower unemployment was an integral component of a better Australia, plus the desire for a higher rate of sustainable economic growth, led to the pursuit of labour policies which have fostered productivity, participation and lower unemployment. Labour and welfare reforms have been particularly important for addressing the various disadvantages that many people face in the labour market and whose employment prospects are less responsive to general increases in labour demand.

Employment arrangements, wages and conditions

Flexible employment arrangements and conditions are more able to promote productivity at the workplace level and to better match employer and employee preferences, a key to good labour market performance and community wellbeing. These more flexible arrangements tend to reduce unemployment, as more people who are unemployed are able to find suitable work.

The Australian workplace relations system has evolved to reflect contemporary economic and social factors. In the early part of the twentieth century, a complex system of awards developed through industrial courts with the objective of equity and justice in wages and working conditions. Unfortunately, over time these complex and rigid institutional arrangements came to inhibit employment outcomes.

Significant reforms were achieved with the *Workplace Relations Act (Cth) 1996*. The Act set primary responsibility for determining matters affecting the relationship between employers and employees with the employer and employees at the workplace level, taking into account the specific circumstances of the individual firm and employees involved. The Act also provided a framework of rights and responsibilities for employers and employees, and their organisations, to support fair and effective agreement-making; ensured freedom of association; and enabled employers and employees to choose the most appropriate form of agreement for their particular circumstances. This included the creation of Australian Workplace Agreements, individual agreements between an employer and employee which would be recognised as legally binding by the Australian Industrial Relations Commission.

These reforms were to significantly redefine the role of awards, with increases in award rates of pay to be modest and focused on the low paid, consistent with the intention that awards operate as a safety net of minimum standards.

As a result of these policy developments, the percentage of workers reliant on arbitrated awards for pay rises has fallen from 67 per cent of employees in 1990 to around 21 per cent in 2002. Around 38 per cent of employees now have their terms and conditions determined through collective agreements between employers and their employees, while another 41 per cent rely on individual agreements reached between an employer and an employee, the latter predominantly being informal arrangements or common law contracts.[12]

While these reforms have focused on encouraging productivity and a more direct relationship between employers and employees, they have had a significant effect on the incentive for employers to hire workers and to boost output, thereby reducing unemployment. The Productivity Commission, for example, has attributed Australia's improved productivity performance in the 1990s in part to better management practices and work arrangements.[13] This has allowed structural reform in product markets to encourage 'the adoption of new production processes and firm organisation, for example through multi-skilling, performance-based remuneration, the introduction of split shifts and the reduced rigidity of job demarcations.'[14] These innovations led to increased competitiveness and a greater capacity for the economy to create employment.

These improvements in flexibility and reduced complexity have also had a supply side effect by creating greater opportunities for people to find jobs, increase their incomes, and respond positively to structural change.

While an improvement in productivity growth was achieved over the 1990s, international comparisons suggest that further improvements in productivity can be made in Australia. As discussed in Statement 4 last year, Australia's productivity level is still below some other major developed nations, particularly the United States.[15] There are a number of aspects to the labour market where further reforms could be made to improve productivity and reduce unemployment.

Workplace agreements, including collective and individual agreements, are considered to be more effective tools for promoting productivity improvements than are awards. However, around 21 per cent of employees remain reliant on awards for determining their conditions of work rather than workplace agreements of some kind. This is one sign that there may be significant potential for the community to further draw on the flexibilities provided by the Workplace Relations Act to achieve higher productivity and employment. While it will be necessary to retain a safety net for many employees, the attractiveness of workplace agreements may increase as the community learns from others' experience in developing agreements and as employers compete for higher quality employees.

Similarly, workplace relations law remains complex and the role of labour law in reducing unemployment could be improved. The Australian Government has over ten bills presently before the Parliament which are designed to increase flexibility, reduce

---

12 *Employee Earnings and Hours* (ABS Cat. No. 6306.0).
13 Cited in OECD (2001), *OECD Economic Surveys — Australia*, Paris, p. 75.
14 OECD (2003), *OECD Economic Surveys — Australia*, p. 84.
15 Australian Government (2003), 'Sustaining Growth in Australia's Living Standards', Budget Paper No. 1, *Budget Strategy and Outlook 2003-04*, Statement 4.

employment transaction costs and achieve a closer link between wages and productivity. More specifically, the proposed amendments to the Workplace Relations Act aim to reduce the degree of regulation around the termination of employment; address pattern bargaining; streamline agreement-making processes; and further simplify awards to promote workplace agreements.

It is important to minimise the employment transaction costs and other on-costs to improve the demand for labour and hence raise employment and reduce unemployment. While employment protection legislation in Australia is generally more refined and less stringent than in other OECD nations,[16] there is scope to improve employment protection law, particularly in relation to small businesses, as existing regulations can be an impediment to these employers taking on additional workers.

Wages are, of course, a key influence on the level of employment. The award system which operates in Australia provides a menu of minimum wages that can significantly affect the employment prospects for unskilled as well as more highly skilled people.

Adult minimum wages in Australia, as a proportion of median earnings, are the second highest in the OECD at around 58 per cent of median earnings. In the United Kingdom and United States, by contrast, minimum wages are around 45 and 34 per cent of median earnings respectively.[17] Australia's award system also provides minimum wages for a range of individual jobs and levels, rather than the single statutory minimum wages that are present in the UK and US jurisdictions. There are around 4,500 industrial awards in operation in Australia, with around 2,000 in the State jurisdictions. These high minimum wages could 'price out' many people from employment and hence result in higher unemployment than otherwise. The rigidities in the wage structure reduce the capacity for wages to adjust to meet labour demand and supply over time.

Governments now intervene more effectively to achieve equity objectives through the tax and welfare systems. By comparison, the award system is a blunt and ineffective mechanism for promoting equity. There may be scope to further refine the award system, including through reductions in its complexity and breadth as well as changes in the responsibilities of the Australian Government and State government jurisdictions.

There will be an ongoing need to review the workplace relations system more broadly to ensure that it meets contemporary and future needs. However, a return to more centralised and less flexible workplace relations, with more extensive powers for third parties such as industrial relations commissions and more regulated employment

---

16 OECD (2003), *OECD Economic Surveys — Australia*, pp. 100-101.

17 OECD data cited in Low Pay Commission (2003), *The National Minimum Wage — Fourth Report of the Low Pay Commission*, London, p. 254.

conditions, would be a regression in policy as it would adversely affect many people in the labour market, including those who are unemployed. A flexible workplace relations system, supported by a safety net of minimum conditions and complementary economic and social policies, can best promote lower unemployment and improved wellbeing.

Skills and capacities

The importance of skills and capacities for labour market performance and wellbeing has become increasingly apparent over time.

The people most likely to be unemployed for sustained periods of time are those who have relatively low education and skills, are of indigenous origin, come from a non-English speaking background or lack labour market experience.[18] Hence, appropriate skills and labour market assistance are necessary to achieve lower unemployment.

Both the level and composition of skills can help in addressing longer-term structural unemployment, which sometimes reflects the declining relevance of some existing skills in the face of economic, technological and social change. New skills can help these people move from unemployment to work, and allow the unemployment rate to fall without creating other pressures in the labour market.

A well-skilled labour force assists the dynamic efficiency of the economy and its ability to expand. In the medium-term, a more appropriately skilled labour force means that as the economy expands there is more likely to be an effective labour supply available and posing less of a wages and inflationary risk to an economic expansion. Over the longer term, a well-skilled labour force can allow the labour market to adjust well to the many forms of structural change and economic dynamics that occur, both boosting economic performance and reducing social dislocation in the face of change.

Over time, governments have developed more active labour market policies which have been found to be more effective than the passive alternatives in getting people into employment.[19] Active labour market policies are in part designed to develop the skills and competencies needed by employers, beyond what have been developed through the mainstream education and training systems. They are targeted at the particular needs of disadvantaged labour market groups and are often remedial or transitional in nature.

---

18 B. Chapman and C. Kapuscinsky (2001), 'The Transformation of Australia's Population, 1970 to 2030: Labour Force, Employment and Unemployment', Centre for Economic Policy Research, Discussion Paper No. 436, Australian National University, Canberra.

19 J. Martin (1998), 'What works among active labour market policies: evidence from OECD countries' experiences', in G. Debelle and J. Borland (eds), *Unemployment and the Australian Labour Market*, proceedings of a conference held by the Reserve Bank of Australia and the Australian National University, Sydney.

By the mid-1980s, labour market programmes had proliferated, with a complex web of options provided for employers and employees and without clear, overarching objectives.[20] As a result, the late 1980s saw some reforms to labour market programmes, with steps taken to achieve a better integration of employment, education and training programmes. In response to the recession of the early 1990s, there was a particular focus on expanding programmes which provided work experience combined with training, in return for income support.[21] For example, the Newstart programme, introduced in 1991 and focused at the outset on the long-term unemployed, introduced obligations on recipients to actively seek work and assisted the acquisition of skills necessary to gain work. However, these programmes were introduced at too late a stage in the economic cycle and in a relatively under-developed form to be effective in quickly redressing the unemployment which emerged as a result of the recession of the early 1990s.

The *Working Nation* package in 1994 saw a significant expansion in labour market programmes, with the development of a case management system for the unemployed, training wages, direct job creation schemes and a Job Compact. The Job Compact guaranteed an education or training place to a long-term unemployed person to enhance their employment prospects. Many of these initiatives were designed to address long-term unemployment, by developing skills and labour market experience.

In the 1996-97 Budget, the Government announced a new framework for the delivery of labour market assistance. The framework was to provide better-quality assistance to unemployed people, target that assistance according to need, address the weaknesses present in the earlier forms of labour market assistance and achieve better value for money. Greater competition in the provision of employment services was introduced, with a greater focus on achieving outcomes for jobseekers.

The framework was centred on a Job Network. Beginning in 1998, Job Network was a national network of private, community and government organisations contracted by the Government to assist unemployed people to find jobs. A government agency, Centrelink, became the gateway to Job Network and undertook the registration, assessment and referral of jobseekers to Job Network members. Over time, the elements of the programme have been developed to better address the varying needs of the unemployed, with mainstream access to the programme supplemented by additional assistance for different categories of disadvantaged jobseekers.

Significant changes were made to the Job Network in 2003, centred on the introduction of an Active Participation Model. The key features of the model have been to provide more intensive assistance the longer a person has been unemployed and a dedicated Job Seeker Account, providing financial support to meet the particular training needs

---

20 Kirby Inquiry (1985), summarised in Committee on Employment Opportunities (1993), *Restoring Full Employment : a discussion paper*, AGPS, Canberra, p. 94.

21 J. Dawkins (1992), *Working for the Future: jobs, skills, innovation*, AGPS, Canberra.

or other expenses involved in getting a person into employment. The model involves stronger linkages between Job Network services and a range of other complementary employment and training programmes, such as the Transition to Work programme and Job Placement Employment and Training.

As a result, a jobseeker now has access to a range of workforce information, education, training and employment services that can be customised to their particular needs in order to get them into sustainable employment. The gains made by the new policy framework have been positive. For instance, the OECD has found that the Job Network has delivered comparable results to those obtained under previous systems but at considerably less cost overall.[22]

While the labour policy framework has evolved over time to provide more effective support, it will be important to ensure that people access the support services that are available to them and that those services work most effectively to meet a person's labour market needs over the short and longer terms. As a result of these policy evolutions, the current system of labour programmes should be better placed to provide support for ongoing employment growth and participation.

As the first section of this Statement illustrated, the flexibility of the Australian labour market is reflected in the ready availability of part-time employment. This flexibility has assisted in reducing the duration of unemployment, as it has provided an avenue for those who have been unemployed for a considerable period of time to develop skills and experience which can then lead to more extensive and continued employment.[23] Without access to part-time employment, many unemployed people may have found it more difficult to gain sustained employment and to become less welfare dependent. This is a key aspect to the effectiveness of labour market programmes, as their objective is to assist unemployed people to find work in a way which places the jobseeker on a path to sustainable employment over the longer term.

Labour market programmes are usually remedial or reactive in nature, drawn upon when they are needed. However, Australian and State governments have focused also on investing in skills as a way of improving a person's labour market prospects. People with a higher level of educational attainment are more likely to participate in the labour force and to be employed than those with lower levels of educational attainment.

Skills and capacities are a key driver of labour force participation, productivity, employment and reductions in unemployment. Solid foundation skills which are adaptable to different circumstances are important for reducing the likelihood of unemployment.

---

22 OECD (2001), *Innovations in Labour Market Policies — the Australian Way*, Paris.

23 Committee on Employment Opportunities (1993), *Restoring Full Employment: a discussion paper*, AGPS, Canberra, p. 2.

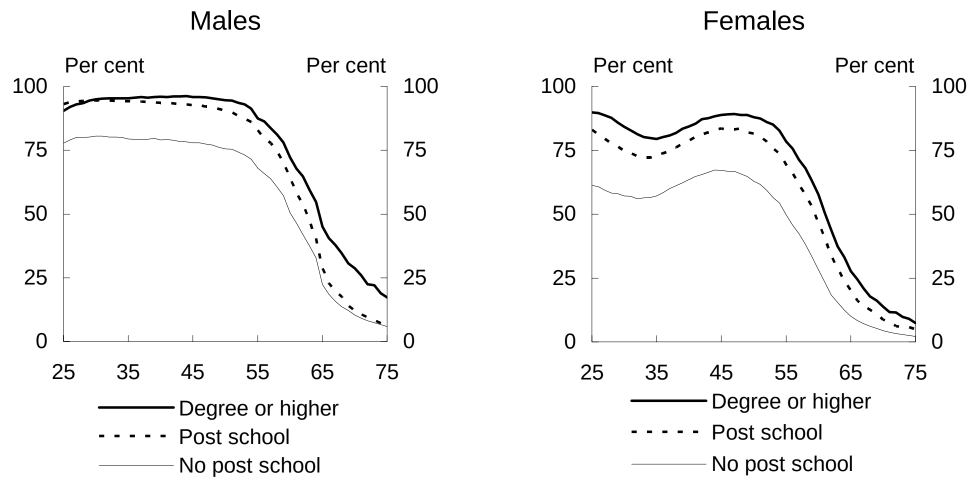
Structural unemployment can be further reduced using the education and training system to better match the skills demanded and supplied in the labour market. In addition, education and training can play a dynamic role in diffusing technologies and promoting innovation, thereby leading to the creation of new industries. Improvements in skills also lead to increased labour mobility which can help to reduce pockets of unemployment in particular regions or occupations.

Those Australians who have not completed secondary school education have a lower labour force participation rate as a group than those with post-secondary qualifications (see Chart 12). This suggests that improving their foundation skills and capacity building could assist in improving employment prospects.

The National Agenda for Early Childhood, initiated in 2003, is one part of the effort to improve foundation skills and capacities to engage in the community, by ensuring that children have a better start in life. A further part of the effort is being made through the National Education Framework for Schools, promoted by the Australian Government to improve the quality of schooling across all key learning areas and to improve the transition to further education and work.

Chart 12: Labour force participation by educational attainment

Per cent of the population age group



Source: S. Kennedy and D. Hedley (2003), 'A Note on Educational Attainment and Labour Force Participation in Australia', Australian Treasury, Working Paper 2003-03.

Education and training policies are also important in ensuring that Australians are able to upgrade their skills over time in order to meet areas of emerging demand for labour. Lifelong learning is important for all workers, whether they have trade qualifications or tertiary qualifications, as it allows people to maintain or improve their productivity, respond to change in the world of work and continue to participate in the labour force.

People with already high educational attainment are more likely to participate in formal training, whether on-the-job or in an educational institution, than those with lower levels of attainment. This may be due to cultural factors and to the various costs of training. For example, significant fees often have to be met by participants up-front without access to financing mechanisms such as those which are available in higher education.[24] As a result, improving equity in access and participation in skill development is a priority for the Government and the Australian National Training Authority.[25]

The skills of the labour force are a function of training as well as the health of the workers involved. Poor occupational health and safety practices, for example, have a significant cost for the Australian economy, through the injuries themselves and the lower levels of participation in the labour force that follow. Hence, improving the health of the labour force will be important for improving productivity and participation, and reducing unemployment.

Reactive health care is expensive relative to preventative health care and, as the population ages, health care costs are expected to rise substantially. Health practices that are focused on preventative health care could mitigate rising health costs but also have substantial benefits in terms of labour force participation and the ability for an individual to continue to engage in employment.

Welfare policies

While skills are an important factor behind labour force participation and the likelihood of employment, welfare and taxation policies also have an effect.

Welfare policies have a substantial effect on the wellbeing of individuals, their households and communities. Greater labour force participation and low unemployment mean that there are higher incomes to draw on. High labour force participation and the minimisation of welfare dependency is better able to create an economically sustainable and inclusive society that is well-connected and better able to manage risks to the economic and social environments.

Policies around publicly-funded income support and income tax arrangements can affect a person's decision to participate in the labour force (and therefore to be employed), along with the extent of their participation. Australia's policies in these areas have changed significantly over the twentieth century, from a comprehensive

24 B. Chapman, L. Watson and L. Wheelahan (2001), 'From silos to seamlessness: towards a cross-sectoral funding model for post-compulsory education and training', Centre for Economic Policy Research, Discussion Paper No. 439, Australian National University, Canberra.

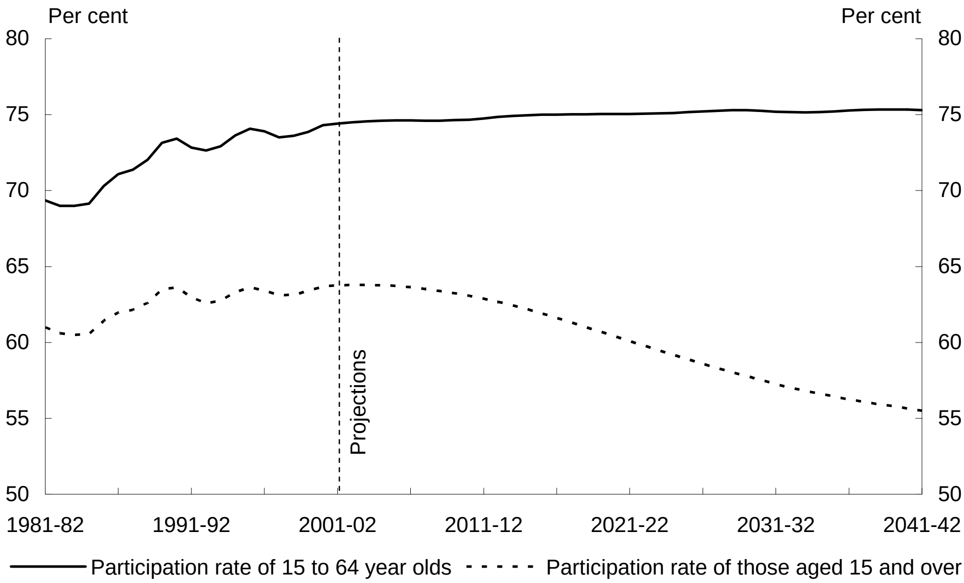
25 Australian National Training Authority (2003), *Shaping Our Future — Australia's national strategy for vocational education and training 2004-2010*, Brisbane.

income support system and wage-earner's welfare state up until the 1980s to a more targeted welfare system in the late 1990s.[26]

The proportion of the Australian working age population in the 55+ age group is rising very significantly and people in that category are less likely to participate in the labour force than those who are below 55 years of age. For example, around 72 per cent of men aged between 55 and 59 years participate in the labour force, compared with 91 per cent of 35 to 44 year olds. Similarly, only 50 per cent of women aged between 55 and 59 years participate in the labour force compared with 71 per cent of 35 to 44 year olds.[27]

The trend towards early retirement, coupled with increasing life expectancy, will have implications for the living standards of all Australians. The community needs to consider how to best provide for its retirement incomes and one readily available solution is to improve labour force participation amongst mature age Australians.

Chart 13: Labour force participation rates by population age category



Source: Australian Government (2002), Budget Paper No. 5, *Intergenerational Report 2002-03.*

Overall labour force participation rates in Australia are also modest in comparison with many other OECD nations, with Australia ranked twelfth highest in the OECD in 2002. In keeping with most other developed countries, Australia's overall participation

---

26 K. Green (2002), 'Welfare reform in Australia and the United States: Tracing the emergence and critiques of the New Paternalism and Mutual Obligation', *The Drawing Board* 3 (1) July, pp. 15-32.

27 OECD (2003), *Labour force statistics, 1982-2002*, Paris.

rate is expected to decline over the long term as the population ages (see Chart 13), even though the participation rate of those of working age is expected to remain broadly stable. That is, the fall in aggregate participation of those aged 15 and over reflects the declining proportion of working age people as Australian society ages.

The effect of population ageing can be illustrated by comparing Australia's and Japan's current situations. The average age of the Japanese population is older than Australia's and participation rates for most age categories are generally similar to or significantly higher than the equivalent age groups in Australia. If Japan had the same age structure as Australia, its labour force participation rate would be some 2 percentage points higher than at present.[28] Hence, the further ageing of the Australian population is projected to have a significant effect on participation and, hence, on growth in national living standards.

Income support is designed to provide a safety net to an individual or family while the primary income earner is out of employment for one reason or another. However, an imbalance between incentives and assistance is a key factor behind structural unemployment. As a result, governments here and abroad have sought to improve the incentives and obligations contained in the income support system.

The Australian income support system for the unemployed was largely designed in the immediate post-World War Two period, when the labour market had very different characteristics to what it has now.

Over time, access to income support has become better targeted according to need, with a reduction in the range of benefits and a tightening of eligibility criteria.

Incentives for some income support recipients to participate were improved through *The New Tax System* and the *Australians Working Together* (AWT) packages. The AWT package in the 2001-02 Budget addressed the principles contained in the 1999 McClure Report on welfare reform, which set out ways in which welfare dependency could be reduced with an overarching aim of assisting out-of-work people back into the workforce. Specific reforms included the introduction of working and training credits; training accounts; as well as other initiatives targeted at parents, the mature-aged, indigenous Australians and people with disabilities — demographic groups which tend to exhibit lower labour force participation rates than other groups, or who are marginally or precariously attached to the labour force.

Reforms announced in the 2001-02 Budget sought to encourage Disability Support Pension recipients to maximise their attachment to the labour market, while similar measures have been introduced for certain Parenting Payment recipients.

---

28 M. Parkinson (2004), 'Growth drivers: the medium to longer-term challenges to maintain Australia's growth performance', address to the Country CFO Forum, Melbourne, 6 February.

The AWT package built on changes that had already been made to the incentive system in the 1997-98 Budget. The Work for the Dole programme attempted to infuse a principle of 'mutual obligation' into the welfare system. Many unemployed people, particularly young people, are now required to undertake community work in return for income support. The programme is predicated on the view that it is fair and reasonable to ask unemployed people to participate in an activity which both helps to improve their employability and makes a contribution to the community in return for payments of unemployment benefits.

Effective marginal tax rates have also been targeted as part of the welfare-work reform agenda. The concept acknowledges that the decision to participate in the labour force, or to actively seek employment if currently unemployed, is affected not only by the additional income taxation paid on earned income but also by the loss of income support payments through income testing arrangements.

The reduction in income tax rates has improved the incentive to work for those on low incomes or on income support, as after-tax income would be higher for an additional hour of work than it otherwise would have been. This substitution effect is particularly strong for those people on relatively low incomes.

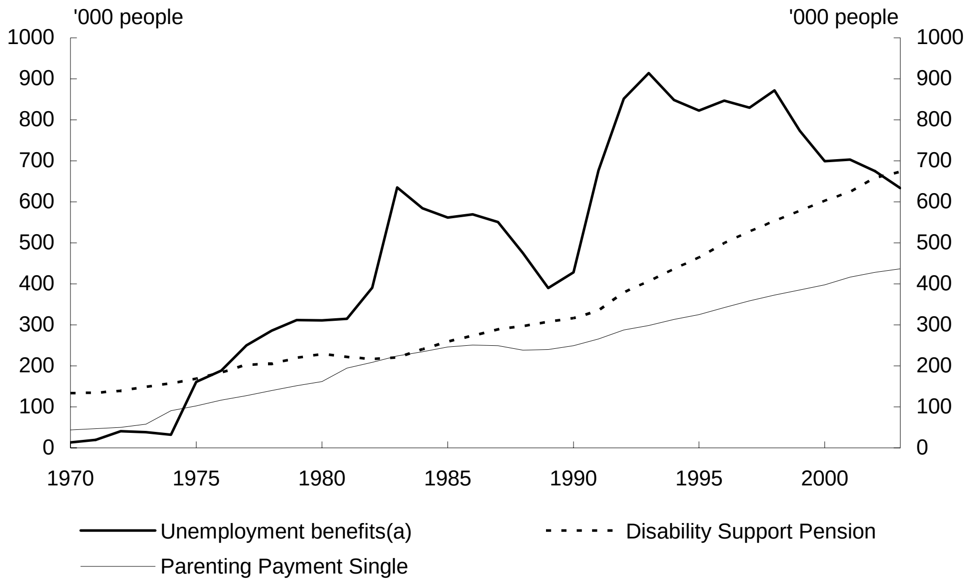
Reductions in effective marginal income tax rates (largely through reduced income tax rates and reduced family assistance taper rates) and an increase in the tax-free income threshold have been delivered at various times since the early 1980s, most significantly through *The New Tax System* reforms in 2002. In its 2003-04 Budget, the Government further reduced income taxation by raising the income thresholds, with the amount of the low income tax offset, and the income threshold from which it starts to phase out, increased. These reforms have allowed income support recipients to retain more of their income support than they would have otherwise been able to do as their employment income rises.

In the 2004-05 Budget, the Government has announced its *More Help for Familie*s package of assistance to families, tax cuts and incentives for saving for retirement. The package builds on the reforms delivered through *The New Tax System* and in the 2003-04 Budget. The package increases the adequacy of assistance for families by increasing the rate of Family Tax Benefits and reducing the withdrawal rates, with improvements in the rewards from work for low and middle income families, and particularly assisting women wishing to re-enter the workforce after having children.

The package also delivers tax cuts by increasing the thresholds for the top two marginal tax rates. This will ensure that high marginal tax rates are not a disincentive for those taking on additional work, wishing to work overtime, seeking promotion, or acquiring skills. The tax cuts will help ensure that Australia is able to retain and attract people with highly regarded skills.

Of Australia's total working age population of around 14 million, only about 10 million are currently part of the labour force.[29] Around 2.7 million working age Australians presently receive income support, representing around 20 per cent of the working age population.[30] Among others, this group includes sole parents and recipients of the Disability Support Pension. There are now more people in receipt of the Disability Support Pension than there are people in receipt of standard unemployment benefits (see Chart 14).

Chart 14: Number of selected income support recipients



Source: Department of Family and Community Services.
(a) Unemployment benefits reflects Newstart Allowance and Youth Allowance (non-students).

Many of these people entered the income support system after becoming unemployed or after having left work voluntarily. Others in this group have sought work but with limited success because of a lack of relevant training or skills, or one or more of the various impediments discussed above. Of the group in receipt of income support, only around a third are subject to an activity test and only half of that group is required to actively look for work. Although many of these people are involved in other important activities, such as education and family-related commitments, there is scope for increasing their attachment to the labour market to improve their longer-term economic and social wellbeing and to realise their potential.

In order to increase Australia's participation rate and further reduce unemployment, it is important that the income support system encourages, promotes and supports people to seek out and participate in paid work to the extent they are able. A balance of

29 *Persons Not in Labour Force* (ABS Cat. No. 6220.0).
30 Australian Government (2004), *Australia's Demographic Challenges*, February.

incentives, assistance and requirements will be needed to maximise the participation of people with diverse capacities and availabilities for work. More consistent arrangements between different forms of income support and better integration of access to programmes that provide active assistance to an individual could assist in improving participation amongst income support recipients.

CONCLUDING COMMENTS

Australia's current unemployment rate is at the lowest sustained level for 23 years, with the rate declining to around 6 per cent in late 2002, and below 6 per cent since late 2003. But unlike other times since the early 1980s when the unemployment rate has declined briefly to 6 per cent or less, the unemployment rate is forecast to remain below 6 per cent on average over the forecast horizon. There also seems to be scope for the unemployment rate to fall even further over the medium term, given ongoing economic growth and further policy reform.

The potential of the labour market to sustain low unemployment is a result of improved macroeconomic policy frameworks and extensive microeconomic reform over a long period of time.

A key theme since the early 1980s has been to increase the 'speed limits' on growth through structural reforms and institutions that are better designed to foster productivity and a sustainable expansion in employment. That process of reform involved decentralising employment arrangements, raising the capacity of the labour force through education and training, developing customised job support and outcomes-focused employment services and creating better incentives in the welfare and taxation systems to promote participation and employment.

Structural reforms have been reinforced in recent years by the adoption of a medium-term framework for the setting of both fiscal and monetary policy in Australia. Coupled with the increased flexibility across the economy flowing from the programme of microeconomic reform, this is helping to make the economy more stable, and less prone to the booms and busts of earlier decades which proved to be a major obstacle to steady and sustainable declines in unemployment.

While unemployment in Australia is now at 23 year lows at less than 6 per cent, some other developed economies have succeeded in pushing unemployment to even lower levels. Labour force participation in Australia is also relatively low compared with some other developed countries, particularly with respect to key age and gender cohorts, such as older males. Hence there is a need to further reform policies to reduce or remove impediments to participate in the labour force and to lower unemployment.

Australia is now moving into a period where it has moderate levels of unemployment but with the onset of new long-term pressures from the ageing of the population. As a result, labour and welfare policies will need to be attuned both to the shorter-term and to these ‘new’ longer-term demands.

The 2004-05 Budget includes a package of major initiatives that address directly these demands through increasing participation and productivity. The package includes measures to further reduce welfare traps for low and middle income families and delivers tax cuts. These will increase rewards from work and increase incentives to take on additional work, seek advancement and acquire skills. This is supplemented by a substantive investment in education, health, innovation and infrastructure.

These initiatives, together with the current solid macroeconomic environment, will enable Australia to achieve lower unemployment and higher labour force participation, provide a higher level of social wellbeing and help deal effectively and sustainably with the ageing of the population.

PART 3
REVENUE, EXPENSES AND BUDGET FUNDING

Statement 5 looks at how the revenue estimates have changed since the 2003-04 Budget and MYEFO. The impact of budget measures is also described.

Statement 6 focuses on short to medium term trends in the expenses and net capital investment estimates. The changes since the 2003-04 Budget and MYEFO are also detailed.

More detail on the budget measures is provided in Budget Paper No. 2.

Statement 7 discusses the Australian Government's debt issuance programme.

STATEMENT 5: REVENUE

This statement contains details of the estimates of Australian Government general government revenue.

The revenue estimates have been revised up since the *Mid-Year Economic and Fiscal Outlook 2003-04* (MYEFO), largely due to stronger expected growth in wages and company profits, partly offset by the Government's decision to provide personal income tax cuts worth $14.7 billion over four years.

Information about GST revenue is provided in Budget Paper No. 3, *Federal Financial Relations 2004-05*.

STATEMENT 5: REVENUE

OVERVIEW

Relative to the *Mid-Year Economic and Fiscal Outlook 2003-04* (MYEFO), total revenue for 2004-05 is expected to be higher, with stronger growth in income tax revenue from wage and salary earners, companies and superannuation funds. Personal income tax cuts of $14.7 billion across the forward estimates will commence from 1 July 2004.

Total revenue

Revenue estimates[1] for the period from 2003-04 to 2007-08 are provided in Table 1.

Table 1: Total Australian Government general government revenue (accrual basis)

	2003-04	2004-05	2005-06	2006-07	2007-08
	Estimate	Estimate	Projection	Projection	Projection
Total taxation revenue ($b)	**174.1**	**182.6**	**190.4**	**200.6**	**211.1**
Real growth on previous year (%)	2.7	2.3	2.3	3.3	3.3
Per cent of GDP	21.5	21.3	21.0	21.0	20.9
Non-taxation revenue ($b)	**12.1**	**10.6**	**11.0**	**11.6**	**12.0**
Real growth on previous year (%)	-2.5	-14.9	2.1	3.7	1.0
Per cent of GDP	1.5	1.2	1.2	1.2	1.2
Total revenue ($b)	**186.2**	**193.2**	**201.4**	**212.2**	**223.1**
Real growth on previous year (%)	2.4	1.2	2.3	3.3	3.1
Per cent of GDP	23.0	22.5	22.2	22.2	22.1

Total revenue is expected to decline from 23.0 per cent of GDP in 2003-04 to 22.1 per cent in 2007-08. Taxation revenue is also expected to decline from 21.5 per cent of GDP in 2003-04 to 20.9 per cent in 2007-08. Historical revenue and receipts outcomes are provided in Appendix F of this statement.

Variations in revenue estimates since 2003-04 Budget

Table 2 is a reconciliation of this Budget's revenue estimates with those at the 2003-04 Budget and MYEFO, in terms of both policy decisions and parameter and other variations.

1 All revenue estimates in this statement are reported on an accrual basis unless otherwise specified. Commentary on accrual and cash taxation revenue is provided on page 5-5 and detailed estimates on a cash basis can be found in Appendix A and Appendix F. The revenue estimates exclude GST revenue, which is collected by the Australian Government and provided in full to the States and Territories. A discussion of GST revenue can be found in Budget Paper No. 3, *Federal Financial Relations 2004-05*.

Table 2: Reconciliation of total Australian Government general government revenue estimates from 2003-04 Budget[(a)] (accrual basis)

	2003-04 $m	2004-05 $m	2005-06 $m	2006-07 $m
2003-04 Budget revenue	**178,325**	**184,991**	**194,244**	**204,715**
Changes between 2003-04 Budget and MYEFO				
Effect of policy decisions	-13	55	207	164
Effect of parameter and other variations	4,343	3,768	5,103	5,586
Total variations	**4,331**	**3,823**	**5,310**	**5,751**
2003-04 MYEFO revenue	**182,655**	**188,814**	**199,554**	**210,466**
Changes between MYEFO and 2004-05 Budget				
Effect of policy decisions	0	-1,796	-3,883	-4,587
Effect of parameter and other variations	3,542	6,133	5,712	6,321
Total variations	**3,541**	**4,337**	**1,829**	**1,734**
2004-05 Budget revenue	**186,197**	**193,151**	**201,383**	**212,199**

(a) The changes in the revenue estimates for 2003-04 and 2004-05 since the 2003-04 MYEFO are summarised by head of revenue at Appendix B.

Total revenue in 2003-04

Since MYEFO, estimated total revenue has been revised up in 2003-04 by $3.5 billion, largely due to higher than expected revenue from wage and salary earners, companies and, to a lesser extent, superannuation funds and small businesses. These increases are expected to be partly offset by lower customs duty.

Total revenue in 2004-05 and the forward years

Total revenue for 2004-05 has been revised up by $4.3 billion since MYEFO. As for 2003-04, the main growth is expected in income taxation revenue from individuals, companies and superannuation funds, with this partly offset by lower customs duty and the impact of the first stage of the Government's personal income tax cuts.

Policy decisions

Policy decisions taken since the 2003-04 MYEFO are expected to reduce revenue by around $1.8 billion in 2004-05 and around $3.9 billion in 2005-06 (a more detailed description of these is provided in Budget Paper No. 2, *Budget Measures 2004-05*).

Most significantly, the Government's decision to provide personal income tax cuts will reduce revenue by $1.9 billion in 2004-05, $3.8 billion in 2005-06 and $14.7 billion over the forward estimates. The tax cuts will take effect in two stages.

- From 1 July 2004, the 42 per cent threshold will be increased from $52,001 to $58,001 and the 47 per cent threshold will be increased from $62,501 to $70,001.

- From 1 July 2005, the 42 per cent threshold will be increased to $63,001 and the 47 per cent threshold will be increased to $80,001.

The Budget also includes a number of other major policy decisions.

- The scheduled reductions in the superannuation surcharge rate will be increased to bring the maximum surcharge rate down to 7.5 per cent by 2006-07, with a cost to revenue of $610 million over the forward estimates.

- A full rebate of wine equalisation tax for $1 million of domestic wholesale sales for wine producers will replace the existing Cellar Door Rebate scheme and accelerated depreciation for grapevine plantings, with a cost to revenue of over $300 million over the forward estimates.

- Additional funding over four years for the Australian Taxation Office for increased compliance activities is expected to result in increased taxation revenue of $251 million in 2004-05 and $1,149 million over the forward estimates period.

- The Australia-United States Free Trade Agreement, expected to come into force in January 2005, will reduce tariff revenue by $190 million in 2004-05 and around $1,460 million over the forward estimates period.

- The application of withholding tax to certain payments made to foreign residents will increase taxation revenue by $125 million in 2004-05 and $540 million over the forward estimates period.

- The Medicare levy thresholds will be increased, in line with the increase in the consumer price index. This will reduce tax revenue by $41 million in 2004-05 and around $100 million over the forward estimates period.

Parameter and other variations

In 2003-04, parameter and other variations are expected to increase estimated revenue by $3.5 billion relative to the MYEFO forecasts.

- Company tax revenue is expected to be $1.7 billion higher, reflecting stronger than expected company profit growth.

- Income tax withholding (ITW) is expected to be $1.1 billion higher, largely due to underlying strength in the labour market.

- Other individuals revenue has been increased by $350 million, driven by strength in small business profitability.

- Customs duty revenue has been reduced by $330 million, due to weaker than expected growth in nominal imports, from the higher exchange rate.

In 2004-05, parameter and other variations are expected to increase revenue by $6.1 billion relative to MYEFO.

- ITW is estimated to increase by $2.3 billion (before the $1.9 billion impact of the personal income tax cuts in that year), reflecting an upward revision to the outlook for wages.
- Company tax revenue has been increased by $1.7 billion, due to a stronger outlook for company profits.
- Superannuation contributions and earnings tax revenue has been increased by around $900 million, reflecting both ongoing strength in superannuation funds contributions and earnings growth and the one-off $610 million impact of the Government's decision to extinguish its liabilities to the Telstra and Australia Post superannuation schemes.
- Revenue from other individuals has been increased by around $290 million, reflecting higher forecast growth for small unincorporated businesses and property income, offset slightly by weaker expected primary producer income.
- Petroleum excise revenue has been estimated to increase by around $240 million, largely due to a higher crude oil price.

Accrual and cash taxation revenue estimates

The revisions to the estimates of cash taxation receipts in this Budget broadly reflect the revisions to estimated accrual taxation revenue. Since MYEFO, estimated cash taxation receipts have been revised up by $2.3 billion in 2003-04, primarily due to higher expected taxation receipts from individuals and companies. For 2004-05, estimated cash taxation receipts have been revised up by $3.4 billion, largely reflecting higher expected taxation receipts from companies and superannuation funds.

The difference between the accrual and cash estimates arises because taxation liabilities are often recognised before the cash payments relating to the liabilities are received. As a result, when revenue is growing, accrual revenue is typically greater than cash receipts. The accrual taxation revenue estimate for 2003-04 is $3.5 billion above the cash taxation receipts estimate, and $2.9 billion above the cash taxation receipts estimate for 2004-05.

More detail on the differences between accrual and cash taxation estimates is provided in Appendix D.

ESTIMATES OF REVENUE

Revenue estimates by revenue head

Table 3: Australian Government general government revenue (accrual basis)

	2003-04 Estimate $m	2004-05 Estimate $m	Change on 2003-04 $m	%
Taxation revenue				
Income taxation				
Individuals and other withholding tax(a)				
Gross income tax withholding	89,870	95,150	5,280	5.9
Gross other individuals	19,760	20,390	630	3.2
less: Refunds	12,200	12,850	650	5.3
Total individuals and other withholding tax	97,430	102,690	5,260	5.4
Companies	37,310	39,400	2,090	5.6
Superannuation funds				
Contributions and earnings	4,510	5,520	1,010	22.4
Superannuation surcharge	1,260	1,390	130	10.3
Total superannuation funds	5,770	6,910	1,140	19.8
Petroleum resource rent tax	1,200	1,100	-100	-8.3
Total income taxation	**141,710**	**150,100**	**8,390**	**5.9**
Indirect taxation				
Excise duty				
Petroleum and other fuel products	13,160	13,320	160	1.2
Crude oil	310	320	10	3.2
Other excise	7,470	7,580	110	1.5
Total excise duty	20,940	21,220	280	1.3
Customs duty	5,585	5,335	-250	-4.5
Other indirect taxes	990	990	0	0.0
Total indirect taxation	**27,515**	**27,545**	**30**	**0.1**
Fringe benefits tax(b)	3,180	3,190	10	0.3
Agricultural levies	561	583	23	4.1
Other taxes	1,116	1,161	45	4.0
Total taxation revenue	**174,082**	**182,580**	**8,498**	**4.9**
Non-taxation revenue	12,115	10,571	-1,543	-12.7
Total revenue	**186,197**	**193,151**	**6,954**	**3.7**

(a) Includes Medicare levy revenue.
(b) Consistent with GFS reporting standards, excludes fringe benefits tax collected from Australian Government agencies (estimated at $364 million in 2003-04 and $380 million in 2004-05).

In 2004-05, total revenue is expected to increase by $7.0 billion, of which taxation revenue is expected to increase by $8.5 billion and non-taxation revenue is expected to decrease by $1.5 billion.

The major contributors to the increase in taxation revenue are a $5.3 billion (5.9 per cent) increase in ITW revenue, a $2.1 billion (5.6 per cent) increase in company tax revenue and a $1.0 billion (22.4 per cent) increase in superannuation contributions and earnings tax revenue (the main part of which is the effect of the Government's payments to Australia Post and Telstra superannuation schemes as set out earlier).

The Budget revenue estimates are strongly influenced by forecast economic growth and the expected composition of economic activity. The stronger outlook for nominal GDP, and company profitability in particular, largely reflects an upward revision to forecast growth in the terms of trade since MYEFO. It is worth noting that the relationship between company profits as measured by the National Accounts and company tax is not a constant one (see Box 1).

The 2004-05 revenue estimates are underpinned by the following major economic assumptions:

- nominal GDP growth of 6 per cent;
- average earnings growth of 4 per cent;
- wage and salary-related employment growth of 1¾ per cent; and
- company income growth of 9¼ per cent.

An analysis of the sensitivity of the revenue estimates to changes in the major economic parameters is provided in Budget Statement 2.

Taxation revenue

Income taxation

Individuals and other withholding tax

Table 4: Individuals and other withholding tax (accrual basis)

	2003-04 Estimate $m	2004-05 Estimate $m	Change on 2003-04 $m	%
Individuals and other withholding tax				
Gross income tax withholding	89,870	95,150	5,280	5.9
Gross other individuals	19,760	20,390	630	3.2
less: Refunds	12,200	12,850	650	5.3
Total individuals and other withholding tax	**97,430**	**102,690**	**5,260**	**5.4**
Includes Medicare levy revenue of:	5,450	5,790	340	6.2

Gross income tax withholding

ITW includes all taxes withheld from payments made under the Pay-As-You-Go (PAYG) withholding system and amounts withheld because no tax file number or Australian business number was quoted. It also includes applicable Medicare levy revenue. The bulk of ITW revenue arises from taxes withheld from wage and salary income but also includes all other withholding taxes levied on natural resource payments, dividends, interest and royalties paid to non-residents and payments to aboriginal groups for the use of land for mineral exploration and mining. These taxes are not separately identified from other PAYG revenues.

ITW revenue is expected to increase by $5.3 billion (5.9 per cent) in 2004-05, an increase of $720 million (0.8 per cent) over revenue forecast at MYEFO.

Gross other individuals

Revenue from other individuals consists of income tax paid by individuals other than that collected through the PAYG withholding system, and includes applicable Medicare levy revenue. It comprises:

- PAYG instalments paid directly by individuals (that is, not withheld by employers); and
- debit assessments on income tax returns.

Taxpayers in this category derive their income from many sources, including:

- profits from small unincorporated businesses, primary production and property investments;
- wages and salaries (when PAYG withholding credits are insufficient to meet the tax liability on assessment); and
- capital gains.

Most revenue from other individuals is collected directly from the taxpayer through the PAYG instalment system. Individuals who are registered for the GST and individuals with tax liabilities of $8,000 or more will generally make quarterly payments. Individuals who are not registered for the GST and have taxation liabilities of less than $8,000 have the choice of making quarterly payments or an annual payment.

Revenue from other individuals is expected to increase by $630 million (3.2 per cent) in 2004-05 reflecting higher forecast growth for small unincorporated businesses and property income, offset slightly by weaker expected primary producer income and the impact of the personal income tax cuts.

Income tax refunds for individuals

A final assessment of the income tax liabilities of individual taxpayers is made on the basis of returns lodged after the end of each financial year. Refunds are made where tax credits exceed the final liability on assessment. Where tax credits are insufficient to meet the final tax liability, taxpayers make an additional payment (a debit assessment), which is recorded under the gross other individuals head of revenue.

Refunds paid to individual income taxpayers in any year will generally relate to earning activity in the prior year because assessment is only made after the conclusion of the year to which it relates.

Refunds to individuals are expected to increase by $650 million (5.3 per cent) in 2004-05. The estimate of growth in refunds for 2004-05 is lower than average, reflecting the impact of the income tax cuts announced in the *2003-04 Budget.*

Medicare levy

Revenue from the Medicare levy is expected to increase by $340 million (6.2 per cent) in 2004-05, broadly consistent with expected growth in wages and employment.

Companies and other related income tax

Table 5: Companies and other related income tax (accrual basis)

	2003-04	2004-05	Change on 2003-04	
	Estimate	Estimate		
	$m	$m	$m	%
Companies	37,310	39,400	2,090	5.6
Superannuation funds				
Contributions and earnings	4,510	5,520	1,010	22.4
Superannuation surcharge	1,260	1,390	130	10.3
Total superannuation funds	5,770	6,910	1,140	19.8
Petroleum resource rent tax	1,200	1,100	-100	-8.3
Total	**44,280**	**47,410**	**3,130**	**7.1**

Company income tax

Company income tax includes all income taxes paid by companies, including incorporated and unincorporated associations, limited partnerships and some public unit trusts. Company tax has been collected through the PAYG instalment system since the financial year beginning 1 July 2000. This system replaced the provisional tax and company tax instalment systems. Under the PAYG instalment system, most company taxpayers now pay their liability through four quarterly instalment payments and a balancing payment (five months after the final instalment), although some small companies are still able to make an annual payment.

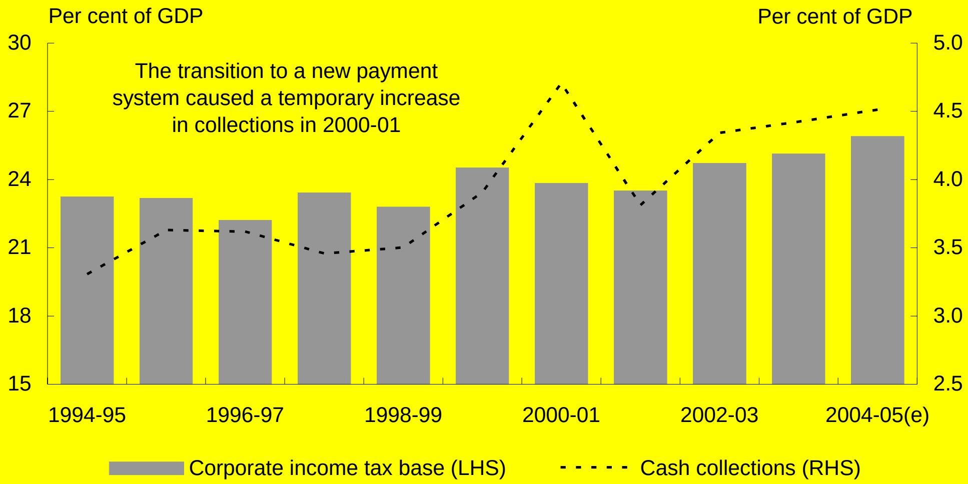
As noted in Appendix D, under the transitional PAYG arrangements, the Government allowed companies to defer some liabilities from the old (pre July 2000) company tax instalment system for up to five years. The cash estimates reflect the expected receipt of these deferred payments ($365 million in 2003-04 and $335 million in 2004-05).

Company tax revenue is expected to increase by $2.1 billion (5.6 per cent) in 2004-05. The estimate has been boosted by a stronger outlook for company profits. This continues the strong growth in company tax collections over recent years. Box 1 provides an analysis of the reasons for this growth.

Box 1: Corporate profitability and company tax collections

Company tax cash collections have increased strongly from 3.3 per cent of GDP in 1994-95 to an estimated 4.5 per cent in 2004-05, around $10.4 billion higher than it otherwise would be. This growth has been underpinned by Australia's long economic expansion and the consequent strong growth in corporate profitability (Chart 1).

Chart 1: Company tax collections and the company income tax base[(a)]



(a) The corporate income tax base is measured as the sum of corporate gross operating surplus, net interest receipts, dividend receipts and a stock valuation adjustment. It does not include an adjustment for depreciation charges.

Several other factors have also contributed to the increase in company tax paid.

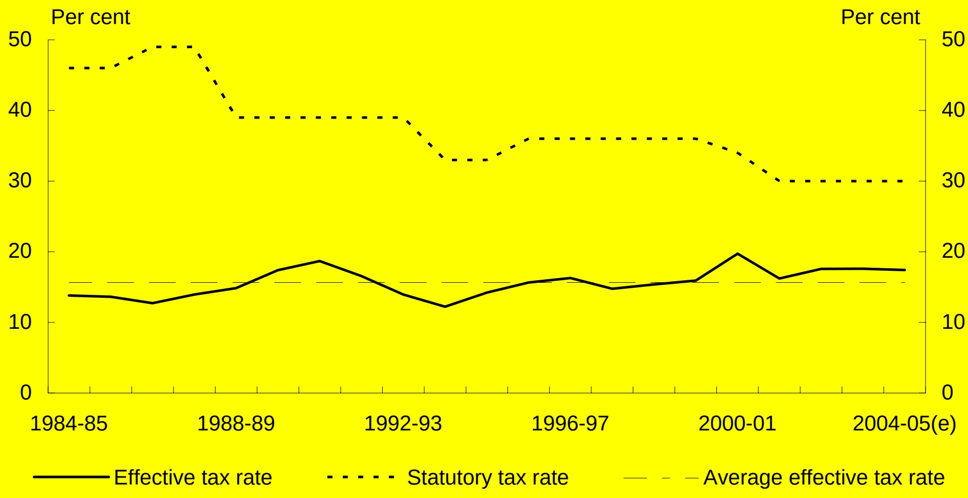
- The privatisation of General Business Enterprises such as Telstra, the Commonwealth Bank of Australia, Victoria Loy Yang A power station and the State Bank of NSW.
- Capital gains tax paid by companies has grown significantly.
- The increasing tendency of small business to incorporate, following the recession of the early 1990s.

In addition, Australia's imputation system may provide some incentive for companies to pay tax in Australia in order to maximise franking credits. In effect, the corporate tax system operates in part as a withholding system for tax due at the shareholder level. Indeed, in recent years the growth of franking credits claimed at the shareholder level has broadly matched the growth in company tax.

Box 1: Corporate profitability and company tax collections (continued)

The strong growth in company tax has arisen despite the reductions in the company tax rate from 36 to 30 per cent, with base-broadening measures in business taxation reform offsetting the reductions in the tax rate, impacting on revenue in a broadly neutral way. In fact, notwithstanding the fall in the statutory tax rate, the effective tax rate (measured as the ratio of tax paid to the corporate income base) has not moved markedly beyond its normal cyclical variation (Chart 2).

Chart 2: Statutory and effective company tax rate



The company loss carry-forward system acts to dampen the cyclical link between corporate profits and taxes paid. However, after a long period of sustained growth in profits, the prior year loss pool will be substantially reduced, and this will cause an increase in tax paid for any given level of profit. This effect may be partly responsible for the small increase in the effective tax rate evident in recent years (as illustrated in Chart 2).

Superannuation funds taxation

Like companies, superannuation funds are taxed through the PAYG instalment system, but at a concessional rate of 15 per cent in relation to taxable contributions received, investment income and capital gains.

Superannuation funds were also allowed to defer some liabilities from the old company tax instalment system for up to five years. The cash estimates reflect the expected receipt of these deferred payments ($25 million in 2003-04 and 2004-05).

Superannuation tax on contributions and earnings income is expected to increase by $1.0 billion (22.4 per cent) in 2004-05, reflecting ongoing strength in superannuation fund contributions and earnings growth and the one-off impact of $610 million from the Government's decision to extinguish its liabilities to the Telstra and Australia Post superannuation schemes. Abstracting from the impact of this decision, the underlying growth rate in superannuation contributions and earnings tax is 8.9 per cent in 2004-05.

A superannuation surcharge is also collected from superannuation funds. In 2003-04, a surcharge of up to 14½ per cent applies to the surchargable contributions of individuals with high incomes. Revenue from the superannuation surcharge is expected to increase by $130 million (10.3 per cent) in 2004-05, reflecting growth in wages. In this Budget, the Government has decided that the surcharge rate will now be reduced to 7.5 per cent by 2006-07.

Petroleum resource rent tax

Petroleum resource rent tax (PRRT) is levied on taxable profits in respect of offshore petroleum projects other than some of the North-West Shelf production and associated exploration areas, which are subject to excise (included in excise on petroleum and other fuel products) and royalties. PRRT is levied at a rate of 40 per cent of taxable profit and the amount paid is deductible from a company's total profit when determining its company tax liability.

PRRT revenue is expected to decrease by $100 million (8.3 per cent) in 2004-05, reflecting an expected decline in production levels offset to some extent by the effect of a higher expected oil price.

Indirect taxation

Table 6: Indirect taxation (accrual basis)

	2003-04 Estimate $m	2004-05 Estimate $m	Change on 2003-04 $m	%
Excise duty				
Petroleum and other fuel products				
Petrol(a)	7,380	7,460	80	1.1
Diesel	5,570	5,630	60	1.1
Other(b)	210	230	20	9.5
Total petroleum and other fuel products	13,160	13,320	160	1.2
Crude oil	310	320	10	3.2
Other excise				
Beer	1,640	1,670	30	1.8
Potable spirits	670	700	30	4.5
Tobacco products	5,160	5,210	50	1.0
Total other excise	7,470	7,580	110	1.5
Total excise	**20,940**	**21,220**	**280**	**1.3**
Customs duty(c)	5,585	5,335	-250	-4.5
Other indirect taxes				
Wine equalisation tax(d)	705	675	-30	-4.3
Luxury car tax	340	330	-10	-2.9
Wholesale sales tax(e)	-55	-15	40	-72.7
Total other indirect taxes	**990**	**990**	**0**	**0.0**
Total	**27,515**	**27,545**	**30**	**0.1**

(a) Includes unleaded petrol and lead replacement petrol.
(b) Includes aviation gasoline, aviation turbine fuel, fuel oil, heating oil and kerosene.
(c) Includes duties imposed on imported petroleum products, tobacco, beer and spirits, which are analogous to excise duty on these items.
(d) Estimates include the offsetting revenue effects of the WET rebate for cellar door and other sales.
(e) WST was abolished on 1 July 2000; however, final liabilities, net of refunds, are still being recognised.

Excise

The major categories of excise duty revenue include petroleum and other fuel products, crude oil, tobacco and alcoholic beverages. Equivalent duties on identical imported products are imposed through, and reported under, customs duty.

Petroleum and other fuel excise includes excise on petrol, diesel fuel, biodiesel, aviation gasoline, aviation turbine fuel, fuel ethanol, fuel oil, heating oil and kerosene. It is imposed at specific rates per litre of product.

- Petrol includes unleaded petrol and lead replacement petrol (which replaced leaded petrol but is taxed at the unleaded petrol rate).
- All revenue from excise duty on aviation gasoline and aviation turbine fuel contributes to the funding of aviation programmes. The rates of excise applying to aviation fuels are adjusted, as necessary, depending on the funding requirements of those programmes.

In 2004-05, revenue from excise on petroleum and other fuel products is estimated to increase by $160 million (1.2 per cent), in line with expected increases in sales of petrol and diesel.

There are two sources of excise on crude oil: production from offshore fields in the North-West Shelf production licence areas which are not subject to PRRT; and production from onshore fields and fields in coastal waters.

- Excise on crude oil is levied on the sale price of the crude oil, and is the only excise not to be levied on a volumetric basis (where excise is applied per unit of quantity).

Revenue from crude oil excise is expected to increase by $10 million (3.2 per cent) in 2004-05.

Other excise is derived from beer, potable spirits and tobacco products.

- For cigarettes, excise is imposed per stick for cigarettes that do not exceed 0.8 grams (actual tobacco content) and a per kilogram basis for other tobacco products.

- For beer, spirits, brandy and ready to drink beverages, excise is imposed on the alcohol content. The excise rate on beer in containers greater than 48 litres (draught beer) is lower than for other beer.

Other excise revenue is expected to increase in 2004-05 by $110 million (1.5 per cent).

Wine is not subject to excise, but is subject to the wine equalisation tax (WET).

Excise indexation

The rates of duty for excisable commodities (with the exception of petroleum products and crude oil) are adjusted every August and February in line with half yearly CPI movements. If the change in the CPI is negative, the excise rate is not reduced but instead the decline is carried forward to offset the next positive CPI movement.

Excise indexation for petroleum products was removed in March 2001.

Table 7: Excise rates

Commodity	Rates applying from 1 Aug 2002 $	Rates applying from 1 Feb 2003 $	Rates applying from 1 Aug 2003 $	Rates applying from 2 Feb 2004 $
Petroleum (per litre)				
Unleaded petrol	0.38143	0.38143	0.38143	0.38143
Diesel	0.38143	0.38143	0.38143	0.38143
Aviation gasoline	0.02808	0.02808	0.03114	0.03114
Aviation turbine fuel	0.02845	0.02845	0.03151	0.03151
Fuel oil	0.07557	0.07557	0.07557	0.07557
Heating oil	0.07557	0.07557	0.07557	0.07557
Kerosene	0.07557	0.07557	0.07557	0.07557
Certain oils, greases and lubricants	0.05449	0.05449	0.05449	0.05449
Beer (per litre of alcohol over 1.15 per cent)				
Draught beer, low strength	5.78	5.86	5.94	6.01
Draught beer, mid strength	18.16	18.41	18.65	18.86
Draught beer, high strength	23.76	24.09	24.40	24.67
Other beer, low strength	28.95	29.36	29.74	30.07
Other beer, mid strength	33.75	34.22	34.66	35.04
Other beer, high strength	33.75	34.22	34.66	35.04
Potable spirits (per litre of alcohol)				
Brandy	53.38	54.13	54.83	55.43
Ready to drink beverages (RTDs)	33.75	34.22	34.66	35.04
General rate for other spirits	57.17	57.97	58.72	59.37
Cigarettes (per stick)	0.21227	0.21524	0.21804	0.22044
Tobacco products (per kg)	265.34	269.05	272.55	275.55

Customs duty

Customs duty is imposed either as a percentage of the value of the imported good or on a volumetric basis (where duty is applied per unit of quantity) for excise equivalent products.

Tariffs on passenger motor vehicles (PMV) and textile, clothing and footwear (TCF) account for around one-third of the total duty collected. A further one-third of customs duty revenue is derived from duty imposed on imports of petroleum products, tobacco, beer and spirits, which is akin to excise duty on these items. The other dutiable goods currently attract a general tariff rate of 5 per cent.

Customs duty is expected to decrease by $250 million (4.5 per cent) in 2004-05. This is due to the combined impact of tariff reductions for PMV and TCF in January 2005, the Australia-United States Free Trade Agreement and more subdued growth in nominal imports due to the higher exchange rate.

Other indirect taxes

Other indirect taxes include the WET, luxury car tax (LCT) and the final wholesale sales tax liability.

All wines, meads, ciders and sakes are subject to the WET rate of 29 per cent, with tax being paid on the wholesale value of the goods. With the proposed rebate for up to $1 million of domestic sales, WET is expected to decline by $30 million (4.3 per cent) in 2004-05.

A LCT of 25 per cent applies to the GST exclusive price of a car above the luxury car tax threshold ($57,009), and there is expected to be a fall in collections of $10 million (2.9 per cent) in 2004-05.

Other indirect taxes are expected to remain unchanged in 2004-05.

Fringe benefits tax and other taxes

Fringe benefits tax

Fringe benefits tax (FBT) is paid on non-salary benefits provided by employers to employees, which are provided in place of, or in addition to, the salary and wages of employees. FBT is payable by employers and is assessed on the value of the fringe benefits provided to employees or their associates. FBT is levied at 48.5 per cent on the grossed-up taxable value of benefits as calculated under the FBT rules. FBT instalments are paid by employers each quarter of the FBT year from April to March (on the Business Activity Statement), with a final balancing payment due in May together with lodgement of the FBT return.

FBT is expected to increase by $10 million (0.3 per cent) in 2004-05.

Agricultural levies and other taxes

Revenue estimates for agricultural levies and other taxes in 2003-04 and 2004-05 are provided in Table 8.

Table 8: Agricultural levies and other taxes (accrual basis)

	2003-04	2004-05	Change on 2003-04	
	Estimate	Estimate		
	$m	$m	$m	%
Agricultural taxes	561	583	23	4.1
Levies, other than agricultural	81	82	1	1.5
Broadcasting licence fees	225	234	9	4.0
Other(a)	810	845	35	4.3
Total	**1,677**	**1,744**	**68**	**4.0**

(a) Includes all other taxation revenue collected by Australian Government agencies.

Total agricultural and other tax revenue is estimated to increase by $68 million (4.0 per cent) in 2004-05. This mainly reflects higher expected revenue from agricultural taxes and the superannuation guarantee charge.

Non-taxation revenue

Revenue estimates for 2003-04 and 2004-05 are provided in Table 9 for the various categories of non-taxation revenue.

Table 9: Non-taxation revenue (accrual basis)

	2003-04	2004-05	Change on 2003-04	
	Estimate	Estimate		
	$m	$m	$m	%
Sales of goods and services	4,192	4,266	74	1.8
Interest				
Interest from other governments	215	202	-13	-6.0
Interest from other sources	1,029	880	-149	-14.5
Total interest	1,244	1,082	-162	-13.0
Dividends				
Dividends from associated entities	4,126	2,543	-1,583	-38.4
Dividends from other sources	45	27	-18	-39.9
Total dividends	4,171	2,570	-1,601	-38.4
Petroleum royalties	558	590	32	5.7
Other non-taxation revenue(a)	1,949	2,063	114	5.9
Total	**12,115**	**10,571**	**-1,543**	**-12.7**

(a) Includes all other non-taxation revenue collected by Australian Government agencies.

Non-taxation revenue is expected to decrease by $1.5 billion (12.7 per cent) in 2004-05. This largely reflects reduced dividend revenue from associated entities.

Sales of goods and services

This category consists of revenue from the direct provision of goods and services by the Australian Government general government sector, including reimbursement of GST administration costs received from the States. Sales of goods and services are expected to increase by $74 million (1.8 per cent) in 2004-05, mainly due to an increase in revenue from GST administration fees and immigration fees.

Interest

Interest income is expected to decrease by $162 million (13.0 per cent) in 2004-05.

Interest from other Governments

This category mainly consists of revenue from the States on General Purpose and Specific Purpose borrowings.

The Australian Government receives interest payments from the States in respect of General Purpose borrowings made on behalf of the States under the State Governments' Loan Council Programme (and from the Northern Territory in respect of advances made under similar general purpose capital assistance arrangements). Payments relating to these advances are made, in turn, by the Australian Government to bond holders.

Interest from the States on General Purpose borrowings is declining as a result of the June 1990 Loan Council decision that the States and Territories make additional payments to the Australian Government each year to facilitate the redemption of all maturing Australian Government securities issued on their behalf. The reduction in interest revenue from the States is matched by a reduction in public debt interest expenses.

The Australian Government also receives interest on Specific Purpose borrowings to the States, including on advances made under the Commonwealth-State Housing Agreements, States (Works and Housing) Assistance Acts, Northern Territory Housing Advances, and by the Australian Capital Territory on debts assumed upon self-government.

Interest from other governments is expected to decrease by $13 million (6.0 per cent) in 2004-05.

Interest from other sources

This item includes interest income on Australian Government cash balances and on other financial assets. It excludes swap transactions entered into as part of the Australian Government's debt management strategy, as they are classified as financing transactions under Government Finance Statistics standards. The Australian Office of Financial Management is responsible for the management and reporting of the Australian Government's net debt portfolio.

Interest income from other sources is expected to decrease by $149 million (14.5 per cent) in 2004-05.

Dividends

The main sources of dividends are the Australian Government's Business Enterprises and the Reserve Bank of Australia (RBA). Dividend payments from the RBA can be volatile, as they are sensitive to movements in interest rates and the exchange rate.

Total dividends are expected to decrease by $1.6 billion (38.4 per cent) in 2004-05, largely due to a decline in RBA dividends. The decrease results from lower estimated earnings due to lower world interest rates and the re-building of RBA foreign exchange reserves.

Petroleum royalties

Petroleum royalties are paid by producers operating in the North-West Shelf oil and gas fields off Western Australia as well as the Timor Sea.

Petroleum royalties are expected to increase by $32 million (5.7 per cent) in 2004-05, due to expected increases in crude oil prices.

Other sources of non-taxation revenue

Other non-taxation revenue includes Child Support Trust Revenue (collected by the Child Support Agency) and seigniorage from circulation coin production.

Other non-taxation revenue is expected to increase by $114 million (5.9 per cent) in 2004-05. There is a $150 million increase due to the recognition of revenue in relation to trust fund receipts from the Reinsurance Trust Fund levies. These levies are imposed by the *Private Health Insurance (Reinsurance Trust Fund Levy) Act 2003*. This revenue is fully offset by an equivalent change in expenses reflecting the payment of the levy into the Trust Fund.

APPENDIX A: FORWARD ESTIMATES OF REVENUE

Table A1: Australian Government revenue (accrual basis)

	2002-03 Actual $m	2003-04 Estimate $m	2004-05 Estimate $m	2005-06 Projection $m	2006-07 Projection $m	2007-08 Projection $m
Taxation revenue						
Income taxation						
Individuals and other withholding tax(a)						
Gross income tax withholding	84,640	89,870	95,150	100,280	107,220	114,490
Gross other individuals	18,314	19,760	20,390	20,940	21,510	22,510
less: Refunds	11,651	12,200	12,850	13,490	14,220	15,140
Total individuals and other withholding tax	91,303	97,430	102,690	107,730	114,510	121,860
Companies	33,365	37,310	39,400	42,230	44,760	47,300
Superannuation funds						
Contributions and earnings	3,617	4,510	5,520	5,290	5,630	6,040
Superannuation surcharge	1,279	1,260	1,390	1,410	1,330	1,190
Total superannuation funds	4,896	5,770	6,910	6,700	6,960	7,230
Petroleum resource rent tax	1,715	1,200	1,100	1,080	1,290	1,190
Total income taxation	**131,278**	**141,710**	**150,100**	**157,740**	**167,520**	**177,580**
Indirect taxation						
Excise duty						
Petroleum and other fuel products	12,920	13,160	13,320	13,460	13,650	13,760
Crude oil	417	310	320	300	290	280
Other excise	7,450	7,470	7,580	7,650	7,770	7,870
Total excise duty	20,787	20,940	21,220	21,410	21,710	21,910
Customs duty	5,573	5,585	5,335	5,149	5,113	5,321
Other indirect taxes	896	990	990	1,050	1,120	1,180
Total indirect taxation	**27,255**	**27,515**	**27,545**	**27,609**	**27,943**	**28,411**
Fringe benefits tax(b)	2,832	3,180	3,190	3,220	3,310	3,410
Agricultural levies	586	561	583	592	594	586
Other taxes	1,104	1,116	1,161	1,216	1,197	1,156
Total taxation revenue	**163,055**	**174,082**	**182,580**	**190,377**	**200,565**	**211,142**
Non-taxation revenue						
Interest received	1,185	1,244	1,082	1,049	1,682	2,556
Dividends and other	10,773	10,870	9,489	9,957	9,953	9,431
Total non-taxation revenue	**11,958**	**12,115**	**10,571**	**11,006**	**11,635**	**11,987**
Total revenue	**175,014**	**186,197**	**193,151**	**201,383**	**212,199**	**223,129**

(a) Includes Medicare levy revenue.
(b) Consistent with GFS reporting standards, excludes fringe benefits tax collected from Australian Government agencies (estimated at $364 million in 2003-04 and $380 million in 2004-05).

Table A2: Australian Government receipts (cash basis)

	2002-03 Actual $m	2003-04 Estimate $m	2004-05 Estimate $m	2005-06 Projection $m	2006-07 Projection $m	2007-08 Projection $m
Taxation receipts						
Income taxation						
Individuals and other withholding tax(a)						
Gross income tax withholding	84,134	89,450	94,400	99,500	106,400	113,610
Gross other individuals	17,436	18,890	19,610	20,170	20,810	21,770
less: Refunds	11,651	12,200	12,850	13,490	14,220	15,140
Total individuals and other withholding tax	89,919	96,140	101,160	106,180	112,990	120,240
Companies	32,752	35,880	38,760	41,640	43,830	46,350
Superannuation funds						
Contributions and earnings	3,865	4,510	5,510	5,280	5,590	6,000
Superannuation Surcharge	975	1,180	1,300	1,320	1,240	1,100
Total superannuation funds	4,840	5,690	6,810	6,600	6,830	7,100
Petroleum resource rent tax	1,712	1,180	1,100	1,080	1,290	1,190
Total income taxation	**129,222**	**138,890**	**147,830**	**155,500**	**164,940**	**174,880**
Indirect taxation						
Excise duty						
Petroleum and other fuel products	12,866	13,170	13,320	13,460	13,650	13,760
Crude oil	417	310	320	300	290	280
Other excise	7,450	7,470	7,580	7,650	7,770	7,870
Total excise duty	20,733	20,950	21,220	21,410	21,710	21,910
Customs duty	4,982	5,020	4,770	4,540	4,540	4,760
Other indirect taxes	858	980	990	1,040	1,110	1,170
Total indirect taxation	**26,573**	**26,950**	**26,980**	**26,990**	**27,360**	**27,840**
Fringe benefits tax(b)	3,103	3,120	3,160	3,250	3,340	3,440
Agricultural levies	586	561	583	592	594	586
Other taxes	1,176	1,023	1,110	1,148	1,147	1,118
Total taxation receipts	**160,661**	**170,544**	**179,663**	**187,480**	**197,381**	**207,864**
Non-taxation receipts						
Interest received	982	1,132	1,014	838	1,357	2,197
Dividends and other	14,504	13,539	13,560	13,513	13,094	12,688
Total non-taxation receipts	**15,487**	**14,671**	**14,574**	**14,351**	**14,451**	**14,884**
Total receipts	**176,147**	**185,214**	**194,237**	**201,831**	**211,832**	**222,748**

(a) Includes Medicare levy receipts.
(b) Consistent with GFS reporting standards, excludes fringe benefits tax collected from Australian Government agencies (estimated at $364 million in 2003-04 and $380 million in 2004-05).

APPENDIX B: CHANGES IN REVENUE SINCE MYEFO

Table B1: Reconciliation of 2003-04 revenue estimates (accrual basis)

	2003-04			
	MYEFO $m	Budget $m	Change on MYEFO $m	Change on MYEFO %
Taxation revenue				
Income taxation				
Individuals and other withholding tax(a)				
Gross income tax withholding	88,750	89,870	1,120	1.3
Gross other individuals	19,410	19,760	350	1.8
less: Refunds	12,300	12,200	-100	-0.8
Total individuals and other withholding tax	95,860	97,430	1,570	1.6
Companies	35,650	37,310	1,660	4.7
Superannuation funds				
Contributions and earnings	4,400	4,510	110	2.5
Superannuation surcharge	1,170	1,260	90	7.7
Petroleum resource rent tax	1,280	1,200	-80	-6.3
Total income taxation	**138,360**	**141,710**	3,350	2.4
Indirect taxation				
Excise duty				
Petroleum and other fuel products	13,140	13,160	20	0.2
Crude oil	250	310	60	24.0
Other excise	7,360	7,470	110	1.5
Total excise duty	20,750	20,940	190	0.9
Customs duty	5,915	5,585	-330	-5.6
Other indirect taxes	920	990	70	7.6
Total indirect taxation	**27,585**	**27,515**	-70	-0.3
Fringe benefits tax(b)	3,150	3,180	30	1.0
Agricultural levies	591	561	-30	-5.1
Other taxes	1,001	1,116	115	11.5
Total taxation revenue	**170,687**	**174,082**	3,395	2.0
Non-taxation revenue	11,969	12,115	146	1.2
Total revenue	**182,655**	**186,197**	3,541	1.9

(a) Includes Medicare levy revenue.
(b) Consistent with GFS reporting standards, excludes fringe benefits tax collected from Australian Government agencies (estimated at $364 million in 2003-04).

Table B2: Reconciliation of 2004-05 revenue estimates (accrual basis)

	2004-05			
	MYEFO $m	Budget $m	Change on MYEFO $m	Change on MYEFO %
Taxation revenue				
Income taxation				
Individuals and other withholding tax(a)				
Gross income tax withholding	94,430	95,150	720	0.8
Gross other individuals	20,220	20,390	170	0.8
less: Refunds	12,930	12,850	-80	-0.6
Total individuals and other withholding tax	101,720	102,690	970	1.0
Companies	37,630	39,400	1,770	4.7
Superannuation funds				
Contributions and earnings	4,590	5,520	930	20.3
Superannuation surcharge	1,200	1,390	190	15.8
Petroleum resource rent tax	920	1,100	180	19.6
Total income tax	**146,060**	**150,100**	4,040	2.8
Indirect taxation				
Excise duty				
Petroleum and other fuel products	13,235	13,320	85	0.6
Crude oil	155	320	165	106.5
Other excise	7,430	7,580	150	2.0
Total excise duty	20,820	21,220	400	1.9
Customs duty	5,825	5,335	-490	-8.4
Other indirect taxes	1,000	990	-10	-1.0
Total indirect taxation	**27,645**	**27,545**	-100	-0.4
Fringe benefits tax(b)	3,090	3,190	100	3.2
Agricultural levies	606	583	-23	-3.8
Other taxes	1,009	1,161	152	15.1
Total taxation revenue	**178,411**	**182,580**	4,169	2.3
Non-taxation revenue	10,403	10,571	168	1.6
Total revenue	**188,814**	**193,151**	4,337	2.3

(a) Includes Medicare levy revenue.
(b) Consistent with GFS reporting standards, excludes fringe benefits tax collected from Australian Government agencies (estimated at $380 million in 2004-05).

APPENDIX C: REVENUE MEASURES

A summary of the revenue measures introduced since MYEFO is provided in Table C1. A full description of these measures can be found in Budget Paper No. 2.

Table C1: Revenue measures since the 2003-04 MYEFO (accrual basis)

	2004-05 $m	2005-06 $m	2006-07 $m	2007-08 $m
ATTORNEY-GENERAL'S				
Australia-United States Free Trade Agreement	-190.0	-400.0	-420.0	-450.0
Portfolio total	**-190.0**	**-400.0**	**-420.0**	**-450.0**
CROSS PORTFOLIO				
Melbourne 2006 Commonwealth Games				
– contribution	-	-1.4	-	-
Portfolio total	**-**	**-1.4**	**-**	**-**
EDUCATION, SCIENCE AND TRAINING				
Investing in Australia's Aged Care				
– better skills for better care	-	..	0.1	0.1
MedicarePlus				
– additional medical school places for Queensland	-	-	..	..
Our Universities				
– Higher Education Loan Programme	11.7	28.1	29.9	26.3
Portfolio total	**11.7**	**28.1**	**29.9**	**26.4**
ENVIRONMENT AND HERITAGE				
Climate Change Strategy				
– continuing administration of the Mandatory Renewable Energy Target	0.5	0.6	0.7	0.9
Portfolio total	**0.5**	**0.6**	**0.7**	**0.9**
FINANCE AND ADMINISTRATION				
Parliamentary superannuation changes	-0.2	-0.6	-0.6	-0.8
Portfolio total	**-0.2**	**-0.6**	**-0.6**	**-0.8**
HEALTH AND AGEING				
Medical Indemnity				
– changes to United Medical Protection liability contributions	-6.7	-9.8	-9.4	-9.4
– run-off reinsurance vehicle	*	*	*	*
Portfolio total	**-6.7**	**-9.8**	**-9.4**	**-9.4**
IMMIGRATION AND MULTICULTURAL AND INDIGENOUS AFFAIRS				
Indigenous Home Ownership Programme				
– expansion	0.5	1.0	1.0	1.0
Migration (non-humanitarian) program	5.8	6.1	6.3	7.0
Regional Migration Initiatives	6.7	14.8	17.5	18.7
Portfolio total	**13.0**	**21.9**	**24.8**	**26.7**

Table C1: Revenue measures since the 2003-04 MYEFO (accrual basis) (continued)

	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m
TREASURY				
A more flexible and adaptable retirement income system				
– allowing people to access their superannuation in the transition to retirement	-	*	*	*
– assets test exemption for income streams	-0.1	-0.2	-0.4	-0.5
– preserving rolled over employer eligible termination payments	*	*	*	*
– removing the requirement for actuarial certificates	-	-	-	-
– removing the work test for superannuation contributions for people under the age of 65	12.8	-34.5	-40.1	-45.9
– requiring compulsory payment of superannuation benefits for people over 75	-1.3	3.3	3.1	3.3
– simplifying the superannuation guarantee notional earnings bases	-10.0	-15.0	-21.0	-24.0
– simplifying the superannuation work test rules for those aged over 65	..	..	..	..
Airservices Australia				
– extension of the Location Specific Pricing subsidy	5.0	2.0	-	-
Australian Prudential Regulation Authority				
– strengthened capabilities	7.4	14.4	11.7	11.9
Australian Securities and Investments Commission				
– enhanced enforcement activities and consumer protection and corporate sector regulation	13.9	15.3	15.8	16.7
Australian Taxation Office				
– taxation and superannuation compliance	251.0	347.8	291.3	259.2
Capital gains tax				
– allowing all insolvency practitioners to declare shares and other securities worthless	*	*	*	*
– excluding input tax credits from the cost base	*	*	*	*
– providing a roll-over on transition to the new superannuation safety arrangements	-	-	-	-
Civil Aviation Safety Authority				
– financial viability	6.5	6.5	6.5	6.5
Consolidation				
– providing greater flexibility	*	*	*	*
Foreign resident withholding				
– requiring withholding from alienated personal services payments	-	-	-	-
– requiring withholding from prescribed payments	125.0	130.0	140.0	145.0
Fringe benefits reporting				
– providing an exclusion for child tuition assistance	..	..	..	..
– providing exclusions for police officers	..	..	..	..
Fringe benefits tax				
– broadening the exemption for the purchase of a new dwelling as a result of relocation	..	..	..	..
– ensuring concessions are available for public ambulance services	-3.0	-4.0	-4.0	-4.0
– extending the transitional arrangements for payments into worker entitlement funds	-	-	-	-

Table C1: Revenue measures since the 2003-04 MYEFO (accrual basis) (continued)

	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m
TREASURY (continued)				
– increasing the thresholds for exempt long service award benefits	..	..	..	..
– providing an exemption for certain benefits received by recipients of military compensation payments	..	..	..	..
Fuel tax reform				
– introducing a new energy content based fuel excise system	-	-	-	-
Interest withholding tax				
– updating of exemptions and the definition of interest	-5.0	-5.0	-5.0	-5.0
Land transport facilities borrowings tax offset				
– phasing down of the scheme	-	-	-	-
Personal income tax				
– reductions in personal income tax	-1,925.0	-3,800.0	-4,250.0	-4,750.0
– increasing the Medicare levy low income thresholds	-41.0	-21.0	-21.0	-21.0
– providing exemptions for certain military compensation payments	..	..	..	..
– simplifying the foreign employment exemption	-	-	-	-
– standardising the dependant child age criteria	-	..	-3.0	-3.0
Petroleum resource rent tax				
– providing an immediate uplift for exploration expenditure in designated offshore frontier areas	-	-2.0	-6.0	-9.0
Philanthropy				
– changing the requirements for the concessional treatment of testamentary gifts and philanthropic funds	-	..	..	..
– creating two new deductible gift recipient categories	-0.5	-1.0	-1.0	-1.0
– implementing the Government's response to the Charities Definition Inquiry	-3.0	-	-	-
– updating the list of eligible deductible gift recipients	*	*	*	*
Small business tax simplification				
– allowing companies more time to repay loans or put loans on a commercial footing	-	*	*	*
– extending depreciating asset roll-over relief for Simplified Tax System partnerships	-	-6.0	-5.0	-5.0
– facilitating movement from annual to quarterly Pay As You Go instalments	-	-	-	-
– facilitating the payment of franked distributions during a private company's first taxable year	-	..	..	..
– increasing flexibility for making family trust and interposed entity elections	-	*	*	*
– providing a fringe benefits tax exemption for additional work-related items	-1.0	-3.0	-4.0	-5.0
– providing a fringe benefits tax exemption for engagement of relocation consultants	*	*	*	*
– removing the customary requirement for the fringe benefits tax remote area housing exemption	-	-2.0	-2.5	-3.0
Superannuation				
– incentives for saving for retirement – surcharge rate reduction	-	-55.0	-170.0	-385.0
– improving the integrity of the superannuation system	*	*	*	*

Table C1: Revenue measures since the 2003-04 MYEFO (accrual basis) (continued)

	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m
TREASURY (continued)				
Superannuation Complaints Tribunal				
– relocation	0.8	0.3	0.3	0.3
Tax losses				
– simplifying the loss recoupment rules for companies	*	*	*	*
Uniform capital allowances				
– allowing deductions for the cost of acquiring certain telecommunications rights	-1.1	-3.2	-4.5	-5.5
Venture capital				
– ensuring the Venture Capital Limited Partnership regime operates as intended	-	-	-	-
Water facilities and landcare tax concessions				
– providing access for irrigation water providers	-	-5.0	-5.0	-5.0
Wine industry assistance				
– providing a wine equalisation tax producer rebate	-58.0	-90.0	-90.0	-100.0
– removing accelerated depreciation of grapevine plantings	2.0	6.0	11.0	17.0
Portfolio total	**-1,624.6**	**-3,521.3**	**-4,152.8**	**-4,912.0**
Decisions taken but not yet announced	-	-	-60.0	-60.0
Total impact of revenue measures	**-1,796.2**	**-3,882.5**	**-4,587.4**	**-5,378.2**

A summary of the revenue measures introduced from the 2003-04 Budget up to MYEFO is provided in Table C2. A full description of these measures can be found in MYEFO.

Table C2: Revenue measures up to the 2003-04 MYEFO (accrual basis)

	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m
ATTORNEY-GENERAL'S				
Australia-Thailand Closer Economic Relations				
– Free Trade Agreement	-90.0	-100.0	-100.0	-110.0
Customs duty				
– changes to Australia's duty free concessions	..	..	..	..
– extension of concessions for goods used in the oil and gas sector	..	..	..	..
– textile, clothing and footwear tariff reductions	-	-	-	-
Textile, clothing and footwear assistance package post-2005				
– extension of the Expanded Overseas Assembly Provision scheme	-	-5.0	-5.0	-5.0
Import Credit Scheme	-	-	-5.0	-5.0
Portfolio total	**-90.0**	**-105.0**	**-110.0**	**-120.0**
COMMUNICATIONS, INFORMATION TECHNOLOGY AND THE ARTS				
Postal Industry Ombudsman				
– establishment	0.3	0.3	0.3	0.3
Regional Telecommunications Inquiry				
– cost recovery for enhanced regional telecommunications monitoring	1.7	1.1	1.2	1.2
Portfolio total	**2.0**	**1.4**	**1.4**	**1.5**
EDUCATION, SCIENCE AND TRAINING				
Our Universities				
– Commonwealth Grants Scheme – increased flexibility	-	0.4	1.1	1.9
enhancements to higher education reform package	-	-	2.4	5.0
– Higher Education Loans Programme (HELP) extension	-	0.1	0.2	0.4
Portfolio total	**-**	**0.4**	**3.7**	**7.4**
HEALTH AND AGEING				
Medical Indemnity				
– Incurred-But-Not-Reported (IBNR) Indemnity Scheme Levy	*	*	*	*
Portfolio total	**-**	**-**	**-**	**-**
TRANSPORT AND REGIONAL SERVICES				
Air Passenger Ticket Levy discontinuation	-	-	-	-
Portfolio total	**-**	**-**	**-**	**-**
TREASURY				
Income tax				
Asset financing arrangements involving tax-preferred entities	*	*	*	*
Capital gains tax				
– demutualisation of friendly societies	..	..	..	..
– preservation of pre-CGT interests in entities that demerge	-	-	-	-
– small business concessions and discretionary trusts	*	*	*	*
Company tax loss recoupment rules	-	-	-	-

Table C2: Revenue measures up to the 2003-04 MYEFO (accrual basis) (continued)

	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m
TREASURY (continued)				
Concessions for Australian Defence Force personnel serving overseas	-	-	-	-
Deductible gift recipients				
– changes to eligible organisations	*	*	*	*
– deductions for contributions with an associated minor benefit	-	-3.0	-3.0	-3.0
Family Tax Benefit				
– income tax deduction for the cost of tax agent fees	-	-	-	-
Farm Management Deposits scheme				
– clarifying eligibility rules	-	-	-	-
Foreign Investment Fund rules				
– additional approved stock exchange	..	..	..	..
Fringe benefits tax				
– transition arrangements for payments to worker entitlement funds	-	-	-	-
Imputation				
– simplified rules for life insurance companies	..	..	..	..
International taxation				
– not proceeding with the foreign income tax exemption for temporary residents	40.0	45.0	45.0	50.0
Superannuation				
– changes to the taxation of overseas superannuation transfers	1.1	0.1	0.1	0.1
– deferral of pension and annuity changes by three months	*	*	*	*
– delayed replacement of the personal superannuation contributions rebate	-	-	-	-
– smaller reduction in the Superannuation Surcharge rate	145.0	205.0	175.0	170.0
Tax administration				
– amendments to the *Crimes (Taxation Offences) Act 1980*	-	-	-	-
– changes to hardship provisions	..	..	..	..
– new civil penalty to deter the promotion of tax avoidance schemes	-	15.0	25.0	35.0
Tax treatment of a payment out of the National Guarantee Fund	-	-	-	-
Taxation of financial arrangements				
– backdating elections under the foreign currency rules	..	-	-	-
– deferral of reforms to commodity hedging taxation arrangements	*	*	*	*
Portfolio total	**186.1**	**262.1**	**242.1**	**252.1**
Decisions taken but not yet announced	-43.0	48.0	27.0	19.0
Total impact of revenue measures	**55.1**	**206.9**	**164.2**	**159.9**

APPENDIX D: ACCRUAL AND CASH TAXATION ESTIMATES

Table D1: Estimates of taxation revenue on an accrual and cash basis

	2003-04	**2004-05**	2005-06	2006-07	2007-08
	$b	**$b**	$b	$b	$b
Taxation revenue (accrual)	174.1	**182.6**	190.4	200.6	211.1
Taxation receipts (cash)	170.5	**179.7**	187.5	197.4	207.9
Difference (accrual less cash)	**3.5**	**2.9**	**2.9**	**3.2**	**3.3**
Memorandum items:					
ACIS(a)	0.6	**0.6**	0.6	0.6	0.6
Deferred company tax payments	-0.4	**-0.4**	-0.4	0.0	0.0
Other	3.4	**2.7**	2.6	2.6	2.7
Total	3.5	**2.9**	2.9	3.2	3.3

(a) Automotive Competitiveness and Investment Scheme

Accrual estimates are prepared using the tax liability method (TLM) of revenue recognition. Under the TLM, taxation revenue is recognised at the time a taxpayer makes a self-assessment or when an assessment of a tax liability is raised by the Australian Taxation Office or the Australian Customs Service. This method retains some elements of cash revenue recognition — for example, revenue is recognised when cash payment occurs prior to an assessment being raised.

Specific drivers of the difference between the accrual and cash taxation revenue estimates are discussed below.

Automotive Competitiveness and Investment Scheme

The Automotive Competitiveness and Investment Scheme (ACIS) operates by providing customs duty credits to exporters of Australian automotive products. The credits can be used to offset future customs duty on specific imports.

Under accrual accounting, an expense is recognised when the ACIS credits are issued. The later redemption of the credits results in an increase in the difference between the accrual and cash estimates for customs duty revenue, because the customs duty accrual revenue is recognised at the point of credit redemption but no cash is received. ACIS credits account for $560 million of the difference between the accrual and cash estimates in 2004-05.

Deferred company tax payments

The PAYG arrangements for companies and superannuation funds (introduced as part of *The New Tax System*) better align tax payments with the period in which income is earned. In the absence of transitional arrangements, this would have created an overlap of tax payments, because payments of tax obligations for 1999-2000 (under the previous payment arrangements) and PAYG instalments for 2000-01 (under the new payment arrangements) both occurred during 2000-01. For a medium-sized company, for example, there would have been six payments due, instead of the usual four.

The Government implemented transitional arrangements to assist these taxpayers move to the new PAYG system, by allowing them to spread some of their tax payments in interest free instalments for up to 5 years. While the full amount of the tax obligations was included in accrual revenue for 2000-01, the year in which the liabilities were recognised, the cash estimates will continue to be affected for the 5 year period, reflecting when the deferred tax payments will be received.

The impact of these deferred payments has been to increase the cash taxation receipt estimates by around $390 million in 2003-04 and $360 million in 2004-05, while they have no impact on the accrual estimates in either year.

Other

This category consists of timing differences between the recognition of accrual and cash revenue and instances where revenue has been recognised but payment is no longer expected to be received. For example:

- *receivables* arise where tax liabilities are recognised in one period, but the taxpayer is not expected to pay the liability until a later period;
- *remissions* occur where tax liabilities are recognised, but circumstances are taken into account and the Commissioner of Taxation reduces the amount of various penalties and interest required to be paid;
- a tax liability may be *written off* where the previously recognised revenue is no longer expected to be received; and
- a *credit amendment* may be issued where a tax assessment is amended (for example, where a court decision leads to a change in the interpretation of the tax laws).

To the extent that revenue includes tax assessments for which payment may not be received, expenses are recognised (that is, in respect of *remissions* and *write-offs* of bad and doubtful debts). The higher revenue is offset by these expenses, leaving the fiscal balance unaffected.

APPENDIX E: TAX EXPENDITURES

This appendix contains a brief overview of the cost of tax concessions provided by the concessional tax treatment of specific activities and/or taxpayers.

Tax concessions provide a benefit to a specified activity or class of taxpayer. Tax concessions can be delivered in a variety of ways, for example by a tax exemption, tax deduction, tax offset, reduced tax rate or by deferring a tax liability. The Government can use tax concessions to allocate resources to different activities or taxpayers in much the same way that it can use direct expenditure programmes. For this reason, and noting their direct impact on the fiscal balance, these tax concessions are generally called tax expenditures.

The data reported in this appendix are consistent with tax expenditure data reported in the *2003 Tax Expenditures Statement* published in January 2004. The Tax Expenditures Statement (TES) is an annual statement of Australian Government tax expenditures.

Table E1 contains estimates of total tax expenditures for the period 2000-01 to 2007-08. There are several considerations that need to be taken into account when analysing tax expenditure data.

- These figures may understate the total cost of tax expenditures, as some identified tax expenditures have not been estimated due to a lack of data and the TES does not necessarily provide a comprehensive listing of all tax expenditures.

- Some caution should be exercised when using these tax expenditure estimates to measure the amount of tax revenue forgone. Tax expenditure estimates measure the benefit of the tax concession to the recipient, not the impact on the fiscal balance from the removal of that tax expenditure. The two might differ due to behavioural responses or for other reasons (see sections 2.1 and 2.5 of the *2003 Tax Expenditures Statement*).

- These figures may overstate the total cost of tax expenditures, as each tax expenditure estimate is an independent calculation of the financial benefits derived by taxpayers that receive that concession, and as such do not generally take into account any inter relationship between tax expenditures.

- Trends in aggregate tax expenditures over time will reflect both changes to the cost of individual tax expenditures and changes in the coverage of tax expenditures being costed.

- Tax expenditure aggregates are net aggregates as they include the offsetting effects of negative tax expenditures.

- Changes over time in methodology and data used to calculate the value of particular tax expenditures can result in large revisions to tax expenditure estimates. Therefore estimates that were provided in previous editions of the TES or in previous Budgets may not be strictly comparable to figures reported here.

Table E1: Aggregate tax expenditures 2000-01 to 2007-08

Year	Superannuation $m	Other tax expenditures $m	Total $m	Tax expenditures as a proportion of GDP (%)
2000-01 (est)	9,685	20,263	29,948	4.5
2001-02 (est)	9,215	20,555	29,770	4.2
2002-03 (est)	10,075	19,946	30,021	4.0
2003-04 (proj)	10,960	19,486	30,446	3.8
2004-05 (proj)	**11,775**	**19,478**	**31,253**	**3.6**
2005-06 (proj)	12,625	19,814	32,439	3.6
2006-07 (proj)	13,450	20,302	33,752	3.5
2007-08 (proj)	14,310	20,849	35,159	3.5

Measured tax expenditures are projected to decline as a proportion of GDP from 4.5 per cent in 2000-01 to around 3.5 per cent in 2007-08. The largest single contributing factor to the decline in total measured tax expenditures is the removal of accelerated depreciation under The New Business Tax System.

APPENDIX F: CASH REVENUE STATISTICS AND HISTORY

Table F1: Australian Government receipts (cash basis)[a]

	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04(b)	2004-05(b)
	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m
Taxation receipts												
Income taxation												
Individuals and other withholding tax(c)												
Gross income tax withholding	47,988	51,831	57,791	62,272	66,842	72,376	77,934	75,009	78,983	84,134	89,450	94,400
Gross other individuals	8,697	9,481	10,078	11,820	12,119	13,103	13,370	13,226	16,290	17,436	18,890	19,610
Gross PPS(d)	1,871	2,169	2,179	2,250	2,524	2,794	3,120	0	0	0	0	0
less: Refunds	7,103	7,931	8,285	8,808	9,525	10,325	10,946	10,989	10,637	11,651	12,200	12,850
Total individuals and other withholding tax	51,452	55,551	61,763	67,533	71,959	77,948	83,478	77,246	84,636	89,919	96,140	101,160
Companies	12,700	15,588	18,252	19,173	19,406	20,734	24,453	31,582	27,230	32,752	35,880	38,760
Superannuation funds												
Contributions and earnings	1,191	1,913	1,634	2,595	2,746	3,630	3,243	4,110	3,550	3,865	4,510	5,510
Superannuation surcharge	0	0	0	0	347	286	577	690	824	975	1,180	1,300
Total superannuation funds	1,191	1,913	1,634	2,595	3,093	3,916	3,820	4,800	4,373	4,840	5,690	6,810
Petroleum resource rent tax	1,072	865	791	1,308	907	419	1,184	2,379	1,361	1,712	1,180	1,100
Total income taxation	**66,416**	**73,916**	**82,440**	**90,610**	**95,366**	**103,017**	**112,936**	**116,006**	**117,601**	**129,222**	**138,890**	**147,830**
Indirect taxation(e)												
Excise duty												
Petroleum and other fuel products	8,499	9,406	10,224	10,543	10,895	10,974	11,189	11,919	12,386	12,866	13,170	13,320
Crude oil and LPG	62	27	13	9	16	31	219	526	393	417	310	320
Other excise	2,253	2,567	2,612	2,739	2,663	2,614	2,670	6,572	6,837	7,450	7,470	7,580
Total excise duty	10,814	12,001	12,849	13,291	13,574	13,619	14,078	19,017	19,616	20,733	20,950	21,220
Customs duty	3,226	3,474	3,124	3,289	3,637	3,634	3,771	4,584	4,625	4,982	5,020	4,770
Other indirect taxes	10,414	11,624	12,955	13,308	14,085	15,162	15,532	1,929	785	858	980	990
Total indirect taxation	**24,455**	**27,099**	**28,928**	**29,888**	**31,296**	**32,415**	**33,381**	**25,530**	**25,026**	**26,573**	**26,950**	**26,980**

Table F1: Australian Government receipts (cash basis)[(a)] (continued)

	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04(b)	2004-05(b)
	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m
Fringe benefits tax	1,417	2,740	3,031	3,163	3,168	3,289	3,373	3,207	3,272	3,103	3,120	3,160
Other taxes	1,736	1,933	1,988	2,154	2,390	2,383	1,005	1,312	1,645	1,762	1,584	1,693
Total taxation receipts	**94,024**	**105,687**	**116,386**	**125,815**	**132,219**	**141,104**	**150,695**	**146,056**	**147,544**	**160,661**	**170,544**	**179,663**
Non-taxation receipts												
Interest received	2,051	1,790	1,403	1,126	1,139	682	995	1,140	918	982	1,132	1,014
Dividends and other	4,671	2,952	3,899	4,089	3,610	4,659	14,116	13,634	14,062	14,504	13,539	13,560
Total non-taxation receipts	**6,722**	**4,743**	**5,302**	**5,216**	**4,749**	**5,341**	**15,111**	**14,774**	**14,980**	**15,487**	**14,671**	**14,574**
Total receipts	**100,747**	**110,430**	**121,688**	**131,031**	**136,968**	**146,444**	**165,806**	**160,829**	**162,524**	**176,147**	**185,214**	**194,237**

(a) Figures up to and including 1998-99 are based on the old Commonwealth Budget Sector cash accounting framework. Figures from 1999-2000 are on an Australian Government general government GFS basis.
(b) Estimates.
(c) Includes the Medicare levy.
(d) PPS denotes Prescribed Payments System, which was replaced by the PAYG withholding system from 1 July 2000.
(e) These items are reported net of Revenue Replacement Payments (RRPs) to the States.

Table F2: Major categories of receipts as a proportion of gross domestic product (cash basis)[(a)]

	Taxation receipts														Non-taxation receipts			
	Income taxation								Other taxation receipts									
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding (b)	Companies	Super funds	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	FBT	Total other tax(c)	Total tax receipts	Interest	Dividends and other	Total non-tax receipts	Total receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
1974-75	10.3	2.4	1.2	11.5	3.5	-	-	15.0	1.0	1.5	1.2	-	5.8	20.7	1.7	0.0	1.7	22.5
1975-76	10.6	2.8	1.7	11.7	3.2	-	-	14.9	1.3	1.6	1.2	-	6.4	21.3	1.7	0.1	1.8	23.1
1976-77	10.8	2.8	1.4	12.2	3.1	-	-	15.2	1.2	1.5	1.3	-	6.3	21.6	1.7	0.2	1.9	23.5
1977-78	10.7	2.5	0.9	12.2	3.1	0.0	-	15.3	1.3	1.4	1.1	-	6.1	21.4	1.8	0.3	2.1	23.5
1978-79	10.2	2.1	0.9	11.4	2.7	0.0	-	14.1	1.9	1.5	1.2	-	6.7	20.7	1.7	0.3	2.0	22.7
1979-80	10.4	2.2	0.9	11.8	2.6	0.0	-	14.4	2.5	1.4	1.2	-	6.9	21.4	1.5	0.3	1.7	23.1
1980-81	10.6	2.3	0.8	12.1	3.2	0.0	-	15.4	2.8	1.2	1.2	-	7.1	22.5	1.5	0.3	1.7	24.2
1981-82	11.3	2.3	0.8	12.7	3.0	0.0	-	15.8	2.5	1.1	1.2	-	6.9	22.6	1.4	0.3	1.8	24.4
1982-83	11.6	2.3	1.1	12.8	2.7	0.0	-	15.5	2.7	1.1	1.1	-	7.3	22.8	1.5	0.5	2.0	24.8
1983-84	11.1	2.2	1.2	12.2	2.2	0.0	-	14.5	2.8	1.0	1.1	-	7.6	22.1	1.5	0.6	2.1	24.1
1984-85	11.5	2.4	0.9	13.2	2.5	0.0	-	15.6	2.9	1.0	1.3	-	8.0	23.6	1.4	0.7	2.1	25.7
1985-86	11.8	2.7	1.4	13.4	2.5	0.0	-	15.9	2.9	1.0	1.3	-	8.0	23.8	1.4	1.0	2.4	26.3
1986-87	12.0	3.2	1.3	14.2	2.5	0.0	-	16.7	2.7	0.9	1.2	0.2	7.9	24.6	1.3	1.1	2.5	27.0
1987-88	11.6	3.2	1.3	13.7	2.8	0.0	-	16.5	2.4	0.9	1.2	0.3	7.8	24.3	1.2	0.8	2.0	26.3
1988-89	11.9	2.8	1.5	13.7	2.9	0.0	-	16.6	2.0	0.6	1.1	0.3	7.2	23.8	1.1	0.3	1.4	25.2
1989-90	11.6	2.7	1.5	13.2	3.4	0.1	0.0	16.7	2.0	0.6	1.0	0.3	7.0	23.7	0.9	0.3	1.2	24.9
1990-91	11.3	2.9	1.7	12.9	3.6	0.3	0.1	16.8	2.0	0.6	0.8	0.3	6.7	23.4	0.8	0.4	1.2	24.7
1991-92	11.0	2.3	1.9	11.7	3.3	0.3	0.2	15.5	1.8	0.6	0.8	0.3	6.1	21.6	0.7	0.6	1.4	23.0
1992-93	10.8	2.0	1.8	11.3	3.1	0.4	0.3	15.1	1.7	0.6	0.8	0.3	5.9	21.0	0.6	0.7	1.3	22.3
1993-94	10.7	1.9	1.6	11.5	2.8	0.3	0.2	14.9	1.9	0.5	0.7	0.3	6.2	21.0	0.5	1.0	1.5	22.5
1994-95	11.0	2.0	1.7	11.8	3.3	0.4	0.2	15.7	2.0	0.5	0.7	0.6	6.7	22.4	0.4	0.6	1.0	23.4
1995-96	11.5	2.0	1.6	12.3	3.6	0.3	0.2	16.4	2.0	0.5	0.6	0.6	6.8	23.1	0.3	0.8	1.1	24.2
1996-97	11.8	2.2	1.7	12.7	3.6	0.5	0.2	17.1	2.0	0.5	0.6	0.6	6.6	23.7	0.2	0.8	1.0	24.7

Table F2: Major categories of receipts as a proportion of gross domestic product (cash basis)[a] (continued)

	Taxation receipts															Non-taxation receipts			
	Income taxation								Other taxation receipts										
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding (b)	Companies	Super funds	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	FBT	Total other tax(c)	Total tax receipts	Interest	Dividends and other	Total non-tax receipts	Total receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
1997-98	11.9	2.2	1.7	12.8	3.5	0.6	0.2	17.0	1.9	0.5	0.6	0.6	6.6	23.6	0.2	0.6	0.8	24.4
1998-99	12.2	2.2	1.7	13.2	3.5	0.7	0.1	17.4	1.9	0.4	0.6	0.6	6.4	23.8	0.1	0.8	0.9	24.7
1999-00	12.4	2.1	1.7	13.3	3.9	0.6	0.2	18.0	1.8	0.4	0.6	0.5	6.0	24.1	0.2	2.3	2.4	26.5
2000-01	11.2	2.0	1.6	11.5	4.7	0.7	0.4	17.3	1.9	1.0	0.7	0.5	4.5	21.8	0.2	2.0	2.2	24.0
2001-02	11.1	2.3	1.5	11.8	3.8	0.6	0.2	16.5	1.8	1.0	0.6	0.5	4.2	20.7	0.1	2.0	2.1	22.8
2002-03	11.2	2.3	1.5	11.9	4.3	0.6	0.2	17.1	1.8	1.0	0.7	0.4	4.2	21.3	0.1	1.9	2.1	23.4
2003-04(d)	11.0	2.3	1.5	11.9	4.4	0.7	0.1	17.1	1.7	0.9	0.6	0.4	3.9	21.0	0.1	1.7	1.8	22.8
2004-05(d)	11.0	2.3	1.5	11.8	4.5	0.8	0.1	17.2	1.6	0.9	0.6	0.4	3.7	20.9	0.1	1.6	1.7	22.6

(a) Figures up to and including 1998-99 are based on the old Commonwealth Budget Sector cash accounting framework. Figures from 1999-2000 are on an Australian Government general government GFS basis.
(b) Also includes gross Prescribed Payments System and Reportable Payments System receipts.
(c) Includes wholesale sales tax, wine equalisation tax, luxury car tax, agricultural levies and other taxes.
(d) Estimates.

Table F3: Major categories of receipts as a proportion of total receipts (cash basis)[(a)]

	Taxation receipts															Non-taxation receipts		
	Income taxation								Other taxation receipts									
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding (b)	Companies	Super funds	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	FBT	Total other tax (c)	Total tax receipts	Interest	Dividends and other	Total non-tax receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
1974-75	45.9	10.8	5.6	51.1	15.5	-	-	66.6	4.6	6.7	5.5	-	25.7	92.3	7.7	0.0	7.7
1975-76	46.1	12.0	7.3	50.7	13.7	-	-	64.5	5.7	6.9	5.1	-	27.7	92.2	7.5	0.3	7.8
1976-77	46.0	11.7	6.0	51.8	13.1	-	-	64.9	5.2	6.3	5.4	-	27.0	91.8	7.4	0.8	8.2
1977-78	45.3	10.5	4.0	51.9	13.1	0.0	-	65.0	5.7	5.9	4.8	-	26.0	91.0	7.6	1.4	9.0
1978-79	44.8	9.3	4.0	50.0	11.8	0.0	-	61.8	8.3	6.6	5.3	-	29.3	91.1	7.4	1.5	8.9
1979-80	45.1	9.6	3.8	50.9	11.4	0.0	-	62.4	10.7	6.0	5.2	-	30.0	92.4	6.4	1.2	7.6
1980-81	43.7	9.7	3.3	50.1	13.3	0.0	-	63.4	11.4	5.1	5.1	-	29.4	92.8	6.1	1.1	7.2
1981-82	46.4	9.2	3.5	52.2	12.3	0.0	-	64.6	10.1	4.5	5.0	-	28.2	92.8	5.9	1.3	7.2
1982-83	46.9	9.1	4.4	51.7	10.8	0.1	-	62.5	10.8	4.5	4.5	-	29.4	91.9	6.1	2.1	8.1
1983-84	45.9	9.1	4.9	50.7	9.3	0.0	-	60.0	11.7	4.3	4.7	-	31.4	91.4	6.0	2.6	8.6
1984-85	44.7	9.4	3.6	51.2	9.6	0.0	-	60.8	11.4	3.7	5.0	-	30.9	91.8	5.5	2.7	8.2
1985-86	45.0	10.3	5.2	51.0	9.4	0.0	-	60.4	10.9	3.6	5.0	-	30.4	90.8	5.3	3.9	9.2
1986-87	44.6	11.8	5.0	52.6	9.1	0.0	-	61.8	9.9	3.5	4.4	0.7	29.2	90.9	4.9	4.2	9.1
1987-88	44.0	12.0	5.1	52.2	10.8	0.0	-	63.0	9.2	3.4	4.5	1.1	29.6	92.5	4.4	3.0	7.5
1988-89	47.3	11.3	5.8	54.4	11.6	0.0	-	65.9	7.9	2.5	4.2	1.1	28.5	94.5	4.2	1.3	5.5
1989-90	46.4	10.8	6.1	53.1	13.5	0.4	0.0	67.0	8.0	2.3	4.1	1.2	28.1	95.2	3.6	1.2	4.8
1990-91	45.8	11.6	6.9	52.2	14.4	1.1	0.3	68.0	8.2	2.4	3.4	1.3	27.1	95.0	3.4	1.6	5.0
1991-92	47.8	9.8	8.3	50.9	14.4	1.2	0.9	67.4	7.7	2.5	3.5	1.4	26.6	94.1	3.2	2.7	5.9
1992-93	48.5	8.8	8.2	50.8	13.7	1.6	1.5	67.6	7.7	2.5	3.5	1.4	26.5	94.1	2.6	3.3	5.9
1993-94	47.6	8.6	7.1	51.1	12.6	1.2	1.1	65.9	8.5	2.2	3.2	1.4	27.4	93.3	2.0	4.6	6.7
1994-95	46.9	8.6	7.2	50.3	14.1	1.7	0.8	66.9	8.5	2.3	3.1	2.5	28.8	95.7	1.6	2.7	4.3
1995-96	47.5	8.3	6.8	50.8	15.0	1.3	0.6	67.7	8.4	2.1	2.6	2.5	27.9	95.6	1.2	3.2	4.4
1996-97	47.5	9.0	6.7	51.5	14.6	2.0	1.0	69.2	8.1	2.1	2.5	2.4	26.9	96.0	0.9	3.1	4.0

Table F3: Major categories of receipts as a proportion of total receipts (cash basis)[(a)] (continued)

	Taxation receipts														Non-taxation receipts		
	Income taxation								Other taxation receipts								
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding (b)	Companies	Super funds	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	FBT	Total other tax (c)	Total tax receipts	Interest	Dividends and other	Total non-tax receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
1997-98	48.8	8.8	7.0	52.5	14.2	2.3	0.7	69.6	8.0	1.9	2.7	2.3	26.9	96.5	0.8	2.6	3.5
1998-99	49.4	8.9	7.1	53.2	14.2	2.7	0.3	70.3	7.5	1.8	2.5	2.2	26.0	96.4	0.5	3.2	3.6
1999-00	47.0	8.1	6.6	50.3	14.7	2.3	0.7	68.1	6.9	1.6	2.3	2.0	22.8	90.9	0.6	8.5	9.1
2000-01	46.6	8.2	6.8	48.0	19.6	3.0	1.5	72.1	7.7	4.1	2.8	2.0	18.7	90.8	0.7	8.5	9.2
2001-02	48.6	10.0	6.5	52.1	16.8	2.7	0.8	72.4	7.9	4.2	2.8	2.0	18.4	90.8	0.6	8.7	9.2
2002-03	47.8	9.9	6.6	51.0	18.6	2.7	1.0	73.4	7.5	4.2	2.8	1.8	17.8	91.2	0.6	8.2	8.8
2003-04(d)	48.3	10.2	6.6	51.9	19.4	3.1	0.6	75.0	7.3	4.0	2.7	1.7	17.1	92.1	0.6	7.3	7.9
2004-05(d)	48.6	10.1	6.6	52.1	20.0	3.5	0.6	76.1	7.0	3.9	2.5	1.6	16.4	92.5	0.5	7.0	7.5

(a) Figures up to and including 1998-99 are based on the old Commonwealth Budget Sector cash accounting framework. Figures from 1999-2000 are on an Australian Government general government GFS basis.
(b) Also includes gross Prescribed Payments System and Reportable Payments System receipts.
(c) Includes wholesale sales tax, wine equalisation tax, luxury car tax, agricultural levies and other taxes.
(d) Estimates.

Statement 6: Expenses and Net Capital Investment

Statement 6 presents estimates of general government expenses and net capital investment on a Government Finance Statistics (GFS) accrual accounting basis. The statement includes information on the allocation of Australian Government funds to the various functions of government. These functions are based on an international standard classification of functions of government that is incorporated into the GFS framework.

The first part of this Statement provides information on trends in expense estimates whilst the second part presents trends in net capital investment estimates. Estimates are on an Australian Government general government sector basis.

Statement 6 focuses on short to medium-term expense trends and their underlying determinants. Consistent with this emphasis, much of Statement 6 explains year-on-year changes across the forward estimates.

Further information on portfolio and agency expenses, capital movements, major outputs and administered items may be found in the respective Portfolio Budget Statements.

The key points are:

- general government expenses are forecast to fall from 22.4 per cent of gross domestic product (GDP) in 2004-05 to 21.9 per cent of GDP in 2007-08;
- in 2004-05, the Social Security and Welfare, Health and Education functions make up just over two-thirds of total expenses — some major trend determinants of long-term growth, for example, population ageing and demand for new technology in the area of health care, were highlighted in the Budget Paper No. 5, Intergenerational Report, 2002-03;
- in real terms, the strongest growth across the Budget and forward estimates years is occurring in the Defence, Education, Social Security and Welfare and Health functions, with other functions in general either being stable or declining; and
- net capital investment is moderately positive in 2004-05 but tends to decline over the forward years as various projects and asset acquisitions come to a conclusion.

CONTENTS

STATEMENT 6: EXPENSES AND NET CAPITAL INVESTMENT

OVERVIEW

Australian Government general government expenses are expected to grow moderately in real terms in 2004-05 (Table 1). Expenses are forecast to fall slightly from 22.6 per cent of gross domestic product (GDP) in 2003-04 to 22.4 per cent of GDP in 2004-05, and are projected to fall as a proportion of GDP over the forward estimates period to 2007-08.

Table 1: Estimates of expenses

	2003-04		2004-05	2005-06	2006-07	2007-08
	MYEFO(a)	Revised	Estimate		Projections	
Total expenses ($b)	**178.9**	**183.1**	**192.3**	**200.6**	**210.0**	**220.9**
Real growth on previous year(%)(b)	3.0	4.0	2.4	2.4	2.7	3.2
Per cent of GDP	22.4	22.6	22.4	22.1	22.0	21.9

(a) As published in the *Mid-Year Economic and Fiscal Outlook 2003-04*.
(b) Real growth is calculated using the non-farm GDP deflator.

GENERAL GOVERNMENT EXPENSES

Reconciliation of expenses since the 2003-04 Budget

Table 2 provides a reconciliation of expense estimates between the 2003-04 Budget, *Mid-Year Economic and Fiscal Outlook 2003-04* (MYEFO) and the 2004-05 Budget, showing the effect of policy decisions and economic parameter and other variations.

Table 2: Reconciliation of expense estimates

	2003-04	2004-05	2005-06	2006-07
	$m	$m	$m	$m
2003-04 Budget expenses	**178,031**	**186,521**	**194,176**	**202,351**
Changes between 2003-04 Budget and MYEFO				
Effect of policy decisions(a)	1,005	1,461	1,224	1,285
Effect of economic parameter variations				
Unemployment benefits	4	4	6	4
Prices and wages	-493	-489	-628	-276
Interest and exchange rates	-342	-384	-404	-456
Total economic parameter variations	*-831*	*-868*	*-1,026*	*-727*
Public debt interest	-122	-71	23	125
Programme specific parameter variations	4	-150	7	248
Slippage in 2003-04 Budget decisions	25	78	96	-41
Other variations	745	601	1,539	1,395
Total variations	**827**	**1,050**	**1,862**	**2,284**
2003-04 MYEFO expenses	**178,858**	**187,571**	**196,039**	**204,635**
Changes between MYEFO and 2004-05 Budget				
Effect of policy decisions(a)	5,969	6,209	6,835	7,766
Effect of economic parameter variations				
Unemployment benefits	-71	-132	-92	-37
Prices and wages	295	393	720	708
Interest and exchange rates	-30	14	90	87
Total economic parameter variations	*194*	*276*	*718*	*757*
Public debt interest	10	94	171	183
Programme specific parameter variations	-600	-777	-879	-861
Slippage in 2003-04 Budget decisions	-9	17	97	121
Other variations	-1,287	-1,085	-2,356	-2,568
Total variations	**4,278**	**4,734**	**4,587**	**5,398**
2004-05 Budget expenses	**183,136**	**192,306**	**200,626**	**210,033**

(a) Excluding the public debt net interest effect of policy measures.

Discussion of the changes between 2003-04 MYEFO and the 2004-05 Budget, shown in the above table can be found in Statement 2 (in the section titled '*Variations in expense estimates*'). Further information on expense measures can be found in Budget Paper No. 2, *Budget Measures 2004-05*.

Expense estimates by function

Table 3 sets out the estimates of Australian Government general government expenses by function for the period 2003-04 to 2007-08.

Table 3: Estimates of expenses by function

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
General public services	10,914	11,864	11,734	11,909	12,307
Defence	13,687	14,425	14,569	15,384	16,423
Public order and safety	2,381	2,727	2,560	2,528	2,485
Education	13,338	14,221	15,024	15,800	16,400
Health	32,355	34,986	36,194	37,763	39,657
Social security and welfare	79,949	82,678	86,995	90,824	94,706
Housing and community amenities	1,652	1,671	1,647	1,624	1,621
Recreation and culture	2,233	2,342	2,417	2,341	2,352
Fuel and energy	3,692	3,922	4,001	3,914	4,036
Agriculture, forestry and fishing	2,158	2,400	1,811	1,665	1,549
Mining, manufacturing and construction	1,717	1,830	1,791	1,705	1,705
Transport and communication	2,731	2,550	2,273	2,437	2,414
Other economic affairs	4,241	4,512	4,556	4,607	4,730
Other purposes	12,088	12,177	15,053	17,533	20,554
Total expenses	**183,136**	**192,306**	**200,626**	**210,033**	**220,939**

Major movements within the estimates of expenses by function between 2003-04 and 2004-05, and across the forward estimates, include increases in the following functions:

- **Defence** due to funding increases flowing from the Government's White Paper *Defence 2000 — Our Future Defence Force* and additional funding being provided in this and previous Budgets for logistics, Defence facilities, military personnel costs and personnel initiatives;
- **Education** due to the impact of indexation arrangements and the announcement of a range of recent policy decisions including increases in funding for higher education, science and innovation and schools;
- **Health** due to a steady increase in the use of medical and pharmaceutical services over the forward estimates period, increasing costs for the provision of medical services and a continuing trend towards newer and more expensive drugs under the Pharmaceutical Benefits Scheme; and
- **Social Security and Welfare** due to the new package of assistance for families — *More help for families*, the on-going effect of indexation of payments, as well as demographic and social factors which affect demand-driven programmes.

Estimates presented in Table 3 above are more fully explained for each individual function in the following pages. Consistent with the short to medium-term focus of Statement 6, analytical commentary focuses on year-on-year changes across the forward estimates.

General public services

Table 4: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Legislative and executive affairs	754	865	746	771	891
Financial and fiscal affairs(a)	3,304	3,445	3,493	3,583	3,519
Foreign affairs and economic aid	2,238	2,465	2,322	2,249	2,375
General research	2,066	2,202	2,394	2,478	2,621
General services	606	674	618	727	741
Government superannuation benefits	1,946	2,213	2,162	2,101	2,160
Total general public services	**10,914**	**11,864**	**11,734**	**11,909**	**12,307**

(a) Debt redemption assistance expenses, paid by the Australian Office of Financial Management to the states and territories under the *Financial Agreement Act 1994*, have been reclassified from the Financial and Fiscal Affairs Sub-function to the Debt Assistance Sub-function (Other Purposes Function).

Nature of expenses and major trends

General public services include expenses on activities concerned with the organisation and operation of government. The function covers legislative and executive affairs, financial and fiscal affairs, foreign economic aid, general research, general services and government superannuation benefits (excluding nominal interest expenses on the unfunded liabilities of Australian Government superannuation schemes which are included under the Nominal Superannuation Interest Sub-function in the Other Purposes Function).

Expenses for the function tend to fluctuate over the budget and forward estimates period partly due to one-off factors such as the preparations for federal elections in 2004-05 and 2007-08 (Legislative and Executive Affairs Sub-function) and the 2006 Census (Financial and Fiscal Affairs Sub-function). General Research Sub-function expenses also grow over the forward estimates period reflecting the on-going impact of the *Backing Australia's Ability – An Innovation Plan for the Future* package, announced in January 2001 and the *Backing Australia's Ability – Building Our Future Through Science and Innovation* package. Increases in the Foreign Affairs and Economic Aid Sub-Function in 2004-05 and 2007-08 are driven by increases in Australia's contributions to multilateral development banks.

Defence

Table 5: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Defence	13,687	14,425	14,569	15,384	16,423
Total defence	**13,687**	**14,425**	**14,569**	**15,384**	**16,423**

Nature of expenses and major trends

Expenses in this function are within the Defence portfolio and support operations and the delivery of navy, army, air and intelligence capabilities and strategic policy in the defence of Australia and its national interests.

Total annual expenses for the Defence Function rise by $2 billion over the period 2004-05 to 2007-08. In real terms, the growth in expenses for this function is 2.4 per cent a year on average.

The growth and pattern of expenses is due to a number of factors. Firstly, there is the influence of significant funding increases for investments in capability announced by the Government in *Defence 2000 – Our Future Defence Force* (the 2000 White Paper). Secondly, there are variations in funding levels for major Australian Defence Force deployments.

The remaining growth in expenses is largely due to additional funding being provided in this and previous budgets for logistics, military personnel costs and personnel initiatives along with Defence's review and refinement of the accounting treatment of expenses and capital to reflect Defence's long-term capital investment programmes. Defence's expenses are partially offset by savings in 2004-05 from the reduction in the cost of equipment purchased overseas due to the appreciation of the Australian dollar.

Public order and safety

Table 6: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Courts and legal services	586	635	629	657	672
Other public order and safety	1,795	2,091	1,931	1,871	1,813
Total public order and safety	**2,381**	**2,727**	**2,560**	**2,528**	**2,485**

Nature of expenses and major trends

Expenses for the Public Order and Safety Function support the administration of the Federal legal system and the provision of legal services, including legal aid, to the community. Public Order and Safety expenses also include law enforcement activities and the protection of Australian Government property.

Expenses for this function peak in 2004-05, reflecting various assistance initiatives in the Pacific. The growth in Other Public Order and Safety Sub-function expenses in 2004-05 reflects the impact of funding for the Regional Assistance Mission to Solomon Islands (RAMSI), and the introduction of the Australia-Papua New Guinea Enhanced Co-operation Programme to help Papua New Guinea address key challenges. Expenses decline from 2005-06 reflecting the fact that various domestic security initiatives and programmes, introduced after the 11 September 2001 and Bali attacks, will require less funding as they move beyond their establishment phase and the year-by-year consideration of RAMSI funding.

The growth in the Courts and Legal Services Sub-function includes measures to maintain equitable access to Commonwealth Legal Aid, establishment of a National Community Crime Prevention Programme, and a one-off increase in resourcing for workload increases in the Attorney-General's Department.

Education

Table 7: Summary of expenses

	2003-04 $m	2004-05 $m	2005-06 $m	2006-07 $m	2007-08 $m
Higher education	4,447	4,735	4,968	5,252	5,296
Vocational and other education	1,417	1,466	1,525	1,517	1,551
Non-government schools	4,450	4,876	5,260	5,639	6,037
Government schools	2,290	2,440	2,596	2,728	2,869
Schools	*6,740*	*7,316*	*7,856*	*8,367*	*8,906*
Student assistance	596	588	561	562	546
General administration	1	1	1	1	1
School education - specific funding	137	114	112	100	101
Total education	**13,338**	**14,221**	**15,024**	**15,800**	**16,400**

Nature of expenses and major trends

Education expenses support the delivery of education services through: higher education institutions; vocational education and training providers (including technical and further education institutions); and government (State and Territory) and non-government schools.

Expenses under the Student Assistance Sub-function include the ABSTUDY scheme, Assistance for Isolated Children and income support for students aged twenty-five years and over through AUSTUDY.

Total expenses for this function are estimated to increase by 8.9 per cent in real terms over the period from 2004-05 to 2007-08, or 2.9 per cent annually on average, with expenses on higher education and schools being the main drivers.

Growth in Higher Education expenses reflect the impact of higher education indexation arrangements and the announcement of policy decisions, including *Our Universities – Backing Australia's Future* announced in the 2003-04 Budget.

Growth in expenses relating to schools is driven by a combination of indexation and the effect of announced policy decisions. Both government and non-government school funding increases according to agreed indexation parameters, incorporated in legislation, which are linked to movements in the Average Government School Recurrent Cost Index. The integration of Catholic systemic schools in the socio-economic status funding model will increase expenses by $356.2 million over four years and a range of measures in this Budget will increase expenses by $160.3 million over four years.

The Student Assistance Sub-function is expected to decline across the forward estimates because of the closure of the Student Financial Supplement Scheme to new borrowers.

Health

Table 8: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Medical services and benefits(a)(b)	13,122	14,154	14,615	15,023	15,457
Hospital services	1,603	1,697	1,837	1,991	2,160
Health care agreements(b)	7,535	7,937	8,331	8,746	9,189
Hospital services and health care agreements	*9,138*	*9,634*	*10,168*	*10,737*	*11,350*
Pharmaceutical services and benefits(b)	6,931	7,593	7,767	8,276	9,036
Aboriginal and Torres Strait Islander health(b)	283	293	301	312	325
Health services(b)	962	1,084	1,028	1,029	1,032
Other health services(b)	1,256	1,473	1,542	1,590	1,635
Other health services	*2,218*	*2,557*	*2,570*	*2,618*	*2,667*
General administration(b)	524	598	611	625	638
Health assistance to the aged(c)	138	156	163	172	183
Total health	**32,355**	**34,986**	**36,194**	**37,763**	**39,657**

(a) The financial impact of premium growth on the forward estimates for the 30 per cent Private Health Insurance Rebate has been allocated to the Contingency Reserve.
(b) The Department of Health and Ageing and the Health Insurance Commission have revised the split of their departmental resourcing across sub-functions and this significantly reduces their impact on the General Administration Sub-function and increases their impact on other health sub-functions.
(c) The bulk of Department of Health and Ageing and Department of Veterans' Affairs expenses for assistance to the aged are now classified to the Assistance to the Aged Sub-function (Social Security and Welfare Function).

Nature of expenses and major trends

The Health Function includes expenses relating to: medical services funded through Medicare and the Private Health Insurance Rebate (Medical Services and Benefits Sub-function); provision of in-hospital services to eligible veterans and their dependants (Hospital Services Sub-function); funding under Australian Health Care Agreements between the Australian Government and the States and Territories (Health Care Agreements Sub-function); and the Pharmaceutical Benefits and Repatriation Pharmaceutical Benefits Schemes (Pharmaceutical Services and Benefits Sub-function).

Expenses related to health are likely to be a major, if not the major, contributor to increased Australian Government spending in the future. Total Government health spending is currently around 4 per cent of GDP.

Health Function expenses are expected to grow on average by around 2.3 per cent per annum in real terms over the budget and forward years. This growth is most pronounced in the areas of medical services and benefits, hospital services and pharmaceutical services and benefits.

Growth in the Medical Services and Benefits Sub-function is largely explained by the increasing costs of medical services, increasing per capita utilisation of medical services, general population growth and the impact of the Government's *MedicarePlus* package.

The trend in the estimates for the Health Care Agreements Sub-function is driven by 3.0 per cent average annual growth, in real terms, in funding for the Australian Health Care Agreements over the life of the new agreements which cover the period 1 July 2003 to 30 June 2008.

Growth in Hospital Services Sub-function expenses is due to an ageing and increasingly frail veteran community requiring more hospital services.

Expenses for the Pharmaceutical Services and Benefits Sub-function are forecast to grow at an average of around 4.0 per cent per annum in real terms, driven by a combination of an ageing population and demand for newer and more expensive drugs (see Box 6.1 below).

Box 6.1: Pharmaceutical Services and Benefits

Table 8.1: Trends in major components of the Pharmaceutical Services and Benefits Sub-function

	2003-04	**2004-05**	2005-06	2006-07	2007-08
	$m	**$m**	$m	$m	$m
Pharmaceutical Benefits (Concessional)(a)	4,195	**4,510**	4,660	4,943	5,420
Pharmaceutical Benefits (General)(a)	1,004	**1,092**	1,131	1,233	1,384
Repatriation Pharmaceutical Benefits Scheme(b)	472	**533**	579	647	720
Highly Specialised Drugs(a)	399	**429**	457	489	520
Other(c)	437	**589**	504	522	546
Sub-total Administered Items	6,507	**7,153**	7,330	7,834	8,590
Departmental Expenses(d)	424	**440**	437	441	446
Total	**6,931**	**7,593**	**7,767**	**8,276**	**9,036**

(a) For a detailed discussion of the Pharmaceutical Benefits Scheme, refer to Outcome 2 of *Health and Ageing 2004-05 Portfolio Budget Statements*.
(b) Veterans' Pharmaceutical Services are covered under Outcome 2 of the *Department of Veterans' Affairs (Defence Portfolio) 2004-05 Portfolio Budget Statements*.
(c) Subsumed within Outcomes 1 and 2 of *Health and Ageing 2004-05 Portfolio Budget Statements*. The decrease in 'Other' from 2004-05 to 2005-06 is attributable to the fulfilment of prevalence cohort immunisations for the *Meningococcal C Vaccination Programme*.
(d) A significant proportion of Health and Ageing Outcome 2 Departmental expenses and approximately half of Health Insurance Commission Departmental expenses are now attributed to this sub-function.

Social security and welfare

Table 9: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Assistance to the aged(a)	27,173	28,460	30,170	31,847	33,720
Assistance to veterans and dependents	5,745	5,993	6,086	6,151	6,226
Assistance to people with disabilities	10,669	11,096	11,810	12,239	12,826
Assistance to families with children	24,489	24,463	25,493	26,584	27,513
Assistance to the unemployed	5,428	5,701	5,733	6,078	6,293
Assistance to the sick	84	86	93	112	128
Assistance to the unemployed and sick	*5,512*	*5,787*	*5,826*	*6,190*	*6,421*
Common youth allowance	2,247	2,318	2,391	2,442	2,513
Other welfare programmes	339	578	1,207	1,351	1,408
Aboriginal advancement nec	1,391	1,502	1,545	1,565	1,582
General administration	2,384	2,480	2,468	2,455	2,496
Total social security and welfare	**79,949**	**82,678**	**86,995**	**90,824**	**94,706**

(a) The bulk of Department of Health and Ageing and Department of Veterans' Affairs expenses for assistance to the aged are classified to this sub-function.

Nature of expenses and major trends

The Social Security and Welfare Function includes pensions and services to the aged, services to the unemployed, assistance to people with disabilities, a variety of assistance to families with children, income support and compensation for veterans and their dependants, and advancement programmes for reconciliation and more generally for Aboriginal and Torres Strait Islander people.

Social Security and Welfare Function expenses are estimated to total around $82.7 billion in 2004-05 and grow significantly over the forward years. There has been a substantial base increase in the Assistance to Families with Children Sub-function in 2003-04, 2004-05 and the forward years due to the new package of assistance to families – *More help for families*. This package includes large increases in Family Tax Benefit Part A assistance, relaxing the income tests for both Family Tax Benefit Part (A) and Family Tax Benefit Part (B), and a new lump sum Maternity Payment.

The sub-functions contributing to the growth in the forward years are the Assistance to the Aged, Assistance to Families with Children and Assistance to People with Disabilities Sub-functions. The main driver for growth in these sub-functions is the indexation of payments, including maintaining the single rate of age and disability pensions at a minimum of 25 per cent of Male Total Average Weekly Earnings (MTAWE) . In addition, demographic and social factors, including the ageing of the population, contribute to growth in the forward year estimates.

Growth across the forward years in the Assistance to the Aged Sub-function is largely due to indexation of the Age Pension, the major component of expenses, by MTAWE. A secondary factor impacting on expenses relating to assistance for the aged is the additional funding for the *Investing in Australia's Aged Care: More Places, Better Care* package.

Growth in the Assistance to Families with Children Sub-function is due to the *More help for families* package and the indexation of the Family Tax Benefit (FTB) Parts A and B, Parenting Payments (partnered and single) and Child Care Benefit.

Similarly, growth in expenses in the Assistance to People with Disabilities Sub-function is driven largely by indexation of major payments including the Disability Support Pension, the Carer Payment, Carer Allowances, and the Commonwealth State Territory Disability Agreement.

Housing and community amenities

Table 10: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Housing	1,227	1,240	1,246	1,263	1,286
Urban and regional development	142	174	142	107	102
Environment protection	284	257	259	254	233
Total housing and community amenities	**1,652**	**1,671**	**1,647**	**1,624**	**1,621**

Nature of expenses and major trends

The Housing and Community Amenities Function includes the Australian Government's contribution to the Commonwealth State Housing Agreement, expenses of the Defence Housing Authority and various regional development and environment protection programmes.

Expenses under the Housing and Community Amenities Function increase in 2004-05 but decrease over the forward years reflecting reductions in expenses in the Urban and Regional Development Sub-function.

This, in turn, reflects the conclusion of funding currently provided for several regional development programmes including the Rural Transaction Centres Programme, the Small Business Interest Rate Relief programmes and the pilot Sustainable Regions Programme.

Expenses for the Environment Protection Sub-function remain relatively stable across 2004-05 to 2007-08 with the Natural Heritage Trust being a major driver.

Other significant expenses on conservation and sustainable use and repair of Australia's natural environment are included in the National Estates and Parks Sub-function (Recreation and Culture Function) and the Natural Resources Development Sub-function (Agriculture, Forestry and Fishing Function).

Recreation and culture

Table 11: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Broadcasting	1,108	1,152	1,164	1,151	1,166
Arts and cultural heritage	713	799	805	808	813
Sport and recreation	206	169	224	159	162
National estate and parks	206	222	224	223	211
Total recreation and culture	**2,233**	**2,342**	**2,417**	**2,341**	**2,352**

Nature of expenses and major trends

Recreation and Culture Function expenses support: public broadcasting; the regulatory framework for Australia's broadcasting sector; cultural institutions; funding for the arts and film industry; assistance to sport and recreation activities; and the management and protection of national parks and other world heritage areas. This function also includes expenses relating to the protection and preservation of historic sites and buildings, including war graves.

Total expenses for the Recreation and Culture Function are steady across the forward estimates period although there are some fluctuations within some sub-functions. The large increases in the Sport and Recreation Sub-function in 2003-04 and 2005-06 reflect the contribution provided to the Victorian Government to assist with the costs associated with staging the 2006 Melbourne Commonwealth Games.

The increase in Arts and Cultural Heritage Sub-function expenses relates to the Refundable Film Tax Offset which is part of the integrated Film Industry Package and provides a 12.5 per cent financial incentive for producers of high-budget films, with qualifying levels of Australian expenditure of at least $15 million per annum, to locate and produce their films in Australia. It also includes a new initiative aimed at strengthening the film and television production sector.

Other significant expenses on conservation and sustainable use and repair of Australia's natural environment are included in the Environment Protection Sub-function (Housing and Community Amenities Function) and the Natural Resources Development Sub-function (Agriculture, Forestry and Fishing Function).

Fuel and energy

Table 12: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Fuel and energy	3,692	3,922	4,001	3,914	4,036
Total fuel and energy	**3,692**	**3,922**	**4,001**	**3,914**	**4,036**

Nature of expenses and major trends

This function includes expenses for the Energy Grants Credits Scheme (EGCS), Cleaner Fuels Grants Scheme and the Fuels Sales Grants Scheme, which are administered by the Australian Taxation Office. The EGCS was introduced on 1 July 2003 and replaced the Diesel Fuel Rebate Scheme and the Diesel and Alternative Fuels Grants Scheme. This function also includes expenses of the Australian Greenhouse Office for programmes funded under *The New Tax System – Measures for a Better Environment Package* and the *Climate Change Strategy* measures. Also included within this function are expenses for programmes relating to the production of alternative fuels including ethanol and biodiesel, that are administered by the Department of Industry, Tourism and Resources and the Australian Taxation Office respectively.

Expenses within this function are expected to increase relatively slowly from 2004-05 to 2007-08. The slow growth in this function and the decline in total expenses in 2006-07 reflect the cessation of the Fuel Sales Grants Scheme. However, significant growth in the EGCS and the impact of the Cleaner Fuels Grants Scheme, decided in the 2003-04 Budget, result in real growth in expenses in 2007-08.

Agriculture, forestry and fishing

Table 13: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Wool industry	57	58	61	61	61
Grains industry	127	131	135	135	135
Dairy industry	267	271	273	275	277
Cattle, sheep and pig industry	113	113	112	112	112
Fishing, horticulture and other agriculture	172	177	180	180	182
General assistance not allocated to specific industries	338	335	270	257	244
Rural assistance	513	675	196	112	54
Natural resources development	388	447	435	387	344
General administration	184	192	150	145	141
Total agriculture, forestry and fishing	**2,158**	**2,400**	**1,811**	**1,665**	**1,549**

Nature of expenses and major trends

Agriculture, Forestry and Fishing Function expenses support assistance to primary producers, forestry, fishing, land and water resources management, quarantine services and contributions to research and development.

Expenses decline over the forward years primarily due to progressively lower expenses within the Rural Assistance and General Assistance Sub-functions. The decline in the Rural Assistance Sub-function after 2004-05 reflects the expected return to normal seasonal conditions in Australia. The decline in the General Assistance Sub-function after 2004-05 reflects the stabilisation of quarantine border controls following a period of higher funding.

Other significant expenses on conservation and sustainable use and repair of Australia's natural environment are included in the Environment Protection Sub-function (Housing and Community Amenities Function) and the National Estate and Parks Sub-function (Recreation and Culture Function).

Manufacturing and mining

Table 14: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Mining, manufacturing and construction	1,717	1,830	1,791	1,705	1,705
Total mining, manufacturing and construction	**1,717**	**1,830**	**1,791**	**1,705**	**1,705**

Nature of expenses and major trends

Expenses under this function relate to the manufacturing and export sectors, and are designed to improve the efficiency and competitiveness of Australian industries. Major expenses include programmes specific to the automotive, textile clothing and footwear (TCF) and pharmaceutical industries. Expenses also include Australian Government assistance to exporters through direct financial assistance for the development of export markets, information and promotional assistance, finance and insurance services, and the development of trade policy. There are also programmes providing research and development assistance grants and a programme of strategic investment incentives.

The increase in expenses in 2004-05 is mainly due to increases in research and development grants and specific strategic investment incentives. The decline in expenses from 2004-05 to 2005-06 is mainly due to a reduction in strategic investment incentives. The further decrease in 2006-07 is due to the renewal and redesign of the TCF programme to more strategically target beneficiaries.

Transport and communication

Table 15: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Communication	412	356	293	250	209
Rail transport(a)	451	3	28	6	0
Air transport	194	158	110	111	111
Road transport(a)	1,372	1,702	1,546	1,777	1,803
Sea transport	201	212	212	212	211
Other transport and communication	101	120	82	82	81
Total transport and communication	**2,731**	**2,550**	**2,273**	**2,437**	**2,414**

(a) Splits of additional AusLink funding between road and rail from 2005-06 onwards are yet to be determined.

Nature of expenses and major trends

Transport and Communication Function expenses support the infrastructure and regulatory framework for Australia's transport and communications sectors.

Expenses fluctuate from 2003-04 to 2007-08 reflecting the irregular expenditure patterns associated with the commencement and/or completion of major programmes or one-off projects. The function includes expenses associated with the Government's new land transport development plan, AusLink, which will involve expenditure on both road and rail for which detailed splits are yet to be determined.

The decline in the Communication Sub-function over the period to 2007-08 reflects the conclusion of programmes associated with several Australian Government initiatives that provided innovative telecommunications infrastructure and services in metropolitan, rural, regional and remote areas of Australia. These included initiatives associated with the sale of the 49.9 per cent of Telstra through two sales of shares in 1997 and 1999 (including the Networking the Nation Programme and the Untimed Local Calls Access Programme), the Telecommunications Service (Besley) Inquiry (including the National Communications Fund and the mobile phones programmes), and the Regional Telecommunications (Estens) Inquiry. The decline is, in part, offset by funding announced as part of the *Backing Australia's Ability — Building Our Future Through Science and Innovation* package.

Rail Transport Sub-function expenses reflect the one-off payment made by the Government to the Australian Trail Track Corporation for new rail infrastructure projects on the interstate rail system in 2003-04. Rail Transport Sub-function expenses will increase from 2004-05 when rail projects to be funded under the new land transport development plan, AusLink are identified.

The Air Transport Sub-function in 2003-04 is higher than 2004-05 and forward years due to a one-off $35 million boost to regional airport security grants.

The impact of AusLink involves an increase in Road Transport expenses from 2004-05 to 2007-08. However, the level of Road Transport expenses in 2004-05 also reflects a one-off $200 million movement of funds from 2002-03 and 2003-04 for the National Highways Programme. AusLink will encompass the National Highways and Roads of National Importance programmes, a redirection of savings from the abolition of the Fuel Sales Grants Scheme to roads funding from 2006-07, increased Government funding of $630 million for the five years to 2008-09, and an extension of the Roads to Recovery Programme for a further four years from 2005-06 to 2008-09, which will provide assistance of $1.2 billion over that period to local councils for the construction, upgrade and maintenance of local roads.

The Government also provides untied funding to local government through Financial Assistance Grants that are identified for roads — see the General Purpose Inter-Government Transactions Sub-function (Other Purposes Function).

Major components of the Road Transport Sub-function are outlined in further detail in Box 6.2 below.

Box 6.2: Components of Road Transport Funding

Table 15.1: Trends in major components of the Road Transport Sub-function

	2003-04 $m	**2004-05 $m**	2005-06 $m	2006-07 $m	2007-08 $m
AusLink(a)					
National Highway and Roads of National Importance	932	**1,247**	1,049	1,011	1,034
Roads to Recovery	302	**253**	300	300	300
Redirection of savings from the abolition of the Fuel Sales Grants Scheme to roads	-	**-**	-	265	270
AusLink Increased Funding(b)	-	**80**	100	150	150
Road Safety Black Spot Programme	45	**45**	45	-	-
Other	93	**77**	52	51	49
Total(c)	**1,372**	**1,702**	**1,546**	**1,777**	**1,803**

(a) Largely Specific Purpose Payments to the States but with a small additional component for land transport research.
(b) Increased funding for AusLink will be available for both road and rail.
(c) See Outcome 1 of the Transport and Regional Services 2004-2005 Portfolio Budget Statements.

Other economic affairs

Table 16: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Tourism and area promotion	142	175	174	163	165
Vocational and industry training	582	616	642	670	711
Labour market assistance to job seekers and industry	1,721	1,798	1,797	1,819	1,876
Industrial relations	271	291	305	307	309
Immigration	743	816	835	853	864
Total labour and employment affairs	*3,317*	*3,521*	*3,578*	*3,649*	*3,760*
Other economic affairs nec	782	816	803	795	804
Total other economic affairs	**4,241**	**4,512**	**4,556**	**4,607**	**4,730**

Nature of expenses and major trends

The Other Economic Affairs Function includes expenses on tourism and area promotion, labour market assistance, immigration, industrial relations and other economic affairs not elsewhere classified (nec).

Expenses over the Budget and forward estimates are relatively stable.

Estimates for the Labour Market Assistance to Job Seekers and Industry Sub-function reflect increases in Job Network Programme funding.

Continuing growth in the Vocational and Industry Training Sub-function is due to an increase in apprenticeship/traineeship commencements.

Other purposes

Table 17: Summary of expenses

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Interest on Australian Government's behalf	3,995	3,881	3,618	3,548	3,593
Interest on behalf of States and Territories	19	11	1	0	0
Interest received on Australian Government stock	0	0	0	0	0
Public debt interest	*4,014*	*3,891*	*3,619*	*3,548*	*3,593*
Nominal superannuation interest	5,155	4,702	5,322	5,446	5,673
General revenue assistance - States and Territories	697	1,122	793	0	0
General capital assistance - States and Territories	0	0	0	0	0
Debt assistance(a)	37	54	196	0	0
Local government assistance	1,511	1,539	1,613	1,675	1,721
Revenue assistance to the States and Territories	156	160	164	168	172
Assistance to other governments	376	393	364	361	369
General purpose inter-government transactions	*2,775*	*3,269*	*3,129*	*2,204*	*2,262*
Natural disaster relief	144	97	97	97	91
Contingency reserve(b)	0	218	2,887	6,238	8,935
Total other purposes	**12,088**	**12,177**	**15,053**	**17,533**	**20,554**

(a) Debt redemption assistance expenses, paid by the Australian Office of Financial Management to the States and Territories under the *Financial Agreement Act 1994*, have been reclassified from the Financial and Fiscal Affairs Sub-function (General Public Services Function) to the Debt Assistance Sub-function.

(b) Asset Sale related expenses are now treated as a component of the Contingency Reserve.

Nature of expenses and major trends

The Other Purposes Function includes expenses incurred in the servicing of public debt interest, and assistance to the State and Territory governments and local government. The function also includes items classified to natural disaster relief, the Contingency Reserve, and costs of asset sales.

Excluding the Contingency Reserve and Nominal Superannuation Interest Sub-functions, the general trend is for a real decline in expenses over the forward years, mainly associated with reductions in Australian Government debt servicing costs — as a result of higher interest bearing debt being settled on maturity and replaced by lower interest bearing debt.

The fall in the General Purpose Inter-Government Transactions Sub-function from 2004-05 reflects trends in Budget Balancing Assistance (BBA) and other payments to the States. BBA payments are expected to cease from 2004-05 onwards as all States are expected to be better off as a result of tax reform in line with increases in GST revenue. However, the estimate for 2004-05 also reflects an Australian Government decision to compensate the States for a measure related to annual lodgement of the GST for some taxpayers.

The decline between 2003-04 and 2004-05 in the nominal superannuation interest expense for civilian superannuation reflects the pay-out of liabilities to the Telstra Superannuation Scheme and the Australia Post Superannuation Scheme. The increase in the nominal interest expense between 2004-05 and 2005-06 reflects the impact of Consumer Price Index movements on the nominal interest rate.

The increase in the Contingency Reserve from 2004-05 over the forward years is largely due to the conservative bias allowance — an allowance that compensates for the trend in expenses on existing Australian Government programmes to be underestimated by agencies in the forward years. The nature of the Contingency Reserve is discussed in more detail at Appendix B.

GENERAL GOVERNMENT NET CAPITAL INVESTMENT

In 2004-05, forecast net capital investment has increased by $463 million since the 2003-04 MYEFO. This increase is due to the combined effect of new policy decisions of $189 million and parameter and other variations of $274 million.

Net capital investment estimates for the period from 2003-04 to 2007-08 are provided in Table 18.

Table 18: Estimates of total net capital investment

	2003-04		2004-05	2005-06	2006-07	2007-08
	MYEFO(a)	Revised	Estimate	Projections		
Total net capital investment ($m)	**-205**	**18**	**148**	**45**	**-125**	**-429**
Real growth on previous year(%)(b)	10.1	107.8	715.3	-70.0	-370.2	-237.8
Per cent of GDP	0.0	0.0	0.0	0.0	0.0	0.0

(a) As published in the *Mid-Year Economic and Fiscal Outlook 2003-04*.
(b) Real growth is calculated using the non-farm gross domestic product (GDP) deflator.

Net capital investment of $18 million is expected in 2003-04, largely reflecting investment in inventory to protect national public health against possible disease outbreaks such as Avian influenza, various construction projects, including activities associated with the construction of a nuclear reactor by the Australian Nuclear Science and Technology Organisation and asset acquisitions and parameter and other effects. Asset acquisitions include: investment by the Department of Finance and Administration in its property portfolio; investment in computer equipment and software by the Australian Customs Service, the Health Insurance Commission and Centrelink; investment in accommodation, transport and communications equipment by the Australian Federal Police; investment in new meteorological radars; and provision of infrastructure in Australia's Indian Ocean territories. These investments are partly offset by ongoing property sales programmes by the Department of Defence and the Defence Housing Authority.

Reconciliation of net capital investment since the 2003-04 Budget

Table 19 provides a reconciliation of the 2003-04 Budget, 2003-04 MYEFO and 2004-05 Budget net capital investment estimates, showing the effect of policy decisions and economic parameter and other variations since the estimates were published in the 2003-04 Budget.

Table 19: Reconciliation of net capital investment

	2003-04	2004-05	2005-06	2006-07
	$m	$m	$m	$m
2003-04 Budget net capital investment	**-417**	**-381**	**-256**	**-448**
Changes between 2003-04 Budget and MYEFO				
Effect of policy decisions	45	18	-3	-3
Effect of parameter and other variations	168	48	130	250
Total variations	**212**	**66**	**127**	**247**
2003-04 MYEFO net capital investment	**-205**	**-315**	**-129**	**-201**
Changes between MYEFO and 2004-05 Budget				
Effect of policy decisions	169	189	151	45
Effect of parameter and other variations	53	274	24	31
Total variations	**222**	**463**	**175**	**76**
2004-05 Budget net capital investment	**18**	**148**	**45**	**-125**

Discussion of changes between the 2003-04 MYEFO and the 2004-05 Budget, shown in the table above, can be found in Statement 2 (in the section titled '*Variations in net capital investment estimates*'). For further information on capital measures since MYEFO can be found in Budget Paper No. 2, *Budget Measures 2004-05*.

Net capital investment estimates by function

Table 20 provides estimates for Australian Government general government net capital investment by function for the period 2003-04 to 2007-08.

Table 20: Estimates of net capital investment by function

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
General public services	94	228	204	34	-13
Defence	-189	-284	-237	-233	-280
Public order and safety	76	103	45	-13	-15
Education	5	2	2	1	0
Health	153	47	10	6	-5
Social security and welfare	31	76	-29	3	-34
Housing and community amenities	-59	9	-80	9	-18
Recreation and culture	-192	2	88	1	-8
Fuel and energy	1	0	0	-1	0
Agriculture, forestry and fishing	2	-1	-2	-11	-3
Mining, manufacturing and construction	5	-1	1	-4	-2
Transport and communications	27	9	5	52	-13
Other economic affairs	38	45	1	9	-22
Other purposes	26	-87	38	22	-16
Total net capital investment	**18**	**148**	**45**	**-125**	**-429**

Net capital investment is expected to rise between 2003-04 and 2004-05 reflecting: various construction projects, including those in the Department of Finance and Administration's property portfolio, investment by the Australian Nuclear Science and Technology Organisation in a new nuclear reactor; investment in information technology by the Australian Customs Service, Centrelink, the Department of Family and Community Services and the Health Insurance Commission; and investment in meteorological radars by the Bureau of Meteorology and equipment by the Australian Federal Police. This is partially offset by receipts received from property sales by the Department of Defence.

While the bulk of Defence's current property sales programme is expected to conclude by 2004-05, rephasing of the Department of Defence's capital investment programme beyond the current forward estimates results in negative net capital investment in the Defence function across the Budget and forward estimates years.

Net capital investment decreases across the forward years as a result of: the rephasing of Defence's capital investment; and the conclusion of various construction projects and information technology-based projects or other asset acquisitions.

Significant investments by function include:

- **General Public Services** for the investment by the Department of Finance and Administration for its property portfolio including construction of the Adelaide Law Courts building, Christmas Island Immigration Reception and Processing Centre, Villawood Detention Centre and ANZAC Park East and West, investment by the Australian Nuclear Science and Technology Organisation in a new nuclear reactor at Lucas Heights and construction, refurbishment and relocation of some overseas posts by the Department of Foreign Affairs and Trade;

- **Public Order and Safety** for investment in computer equipment and software by the Australian Customs Service, including for the Cargo Management Re-engineering Programme, and investment in accommodation, transport and communications equipment associated with overseas deployments by the Australian Federal Police;

- **Health** for investment in inventory to protect national public health against possible disease outbreaks such as Avian influenza, and for investment in information technology infrastructure by the Health Insurance Commission;

- **Social Security and Welfare** for investment in information technology infrastructure for Centrelink;

- **Recreation and Culture** due to the sale of three FM radio broadcasting licenses in 2003-04, delays in the divestment of Australian Broadcasting Corporation properties at Adelaide Terrace in Perth and at Gore Hill in Sydney, capital works at the Australian Institute of Sport and the National Gallery of Australia and the redevelopment of the Australian War Memorial's post-1945 galleries;

- **Housing and Community Amenities** due mainly to changes within the Defence Housing Authority's property portfolio including increased acquisitions and construction and variations to the forecast sale and leaseback programme;

- **Transport and Communications** for the provision of infrastructure on the Indian Ocean Territories and for investment in information technology infrastructure in the Department of Transport and Regional Services, the Civil Aviation and Safety Authority, and the Australian Communications Authority; and

- **Other Economic Affairs** for investment by the Bureau of Meteorology in replacing older equipment with new meteorological radars and by the Department of Immigration and Multicultural and Indigenous Affairs for upgrade, development and redevelopment work associated with immigration detention facilities.

APPENDIX A: EXPENSE ESTIMATES BY FUNCTION AND SUB-FUNCTION

Table A1: Estimates of expenses by function and sub-function

	Actuals	Estimates		Projections		
	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m	$m
General public services						
Legislative and executive affairs	732	754	865	746	771	891
Financial and fiscal affairs(a)	3,476	3,304	3,445	3,493	3,583	3,519
Foreign affairs and economic aid	2,334	2,238	2,465	2,322	2,249	2,375
General research	1,790	2,066	2,202	2,394	2,478	2,621
General services	566	606	674	618	727	741
Government superannuation benefits	2,090	1,946	2,213	2,162	2,101	2,160
Total general public services	**10,988**	**10,914**	**11,864**	**11,734**	**11,909**	**12,307**
Defence	**13,307**	**13,687**	**14,425**	**14,569**	**15,384**	**16,423**
Public order and safety						
Courts and legal services	589	586	635	629	657	672
Other public order and safety	1,378	1,795	2,091	1,931	1,871	1,813
Total public order and safety	**1,968**	**2,381**	**2,727**	**2,560**	**2,528**	**2,485**
Education						
Higher education	4,017	4,447	4,735	4,968	5,252	5,296
Vocational and other education	1,323	1,417	1,466	1,525	1,517	1,551
Non-government schools	3,869	4,450	4,876	5,260	5,639	6,037
Government schools	2,143	2,290	2,440	2,596	2,728	2,869
Schools	*6,013*	*6,740*	*7,316*	*7,856*	*8,367*	*8,906*
Student assistance	641	596	588	561	562	546
General administration	0	1	1	1	1	1
School education - specific funding	115	137	114	112	100	101
Total education	**12,109**	**13,338**	**14,221**	**15,024**	**15,800**	**16,400**
Health						
Medical services and benefits	11,726	13,122	14,154	14,615	15,023	15,457
Hospital services	1,537	1,603	1,697	1,837	1,991	2,160
Health care agreements	7,240	7,535	7,937	8,331	8,746	9,189
Hospital services and health care agreements	*8,776*	*9,138*	*9,634*	*10,168*	*10,737*	*11,350*
Pharmaceutical services and benefits	5,732	6,931	7,593	7,767	8,276	9,036
Aboriginal and Torres Strait Islander health	209	283	293	301	312	325
Health services	667	962	1,084	1,028	1,029	1,032
Other health services	892	1,256	1,473	1,542	1,590	1,635
Other health services	*1,559*	*2,218*	*2,557*	*2,570*	*2,618*	*2,667*
General administration	1,333	524	598	611	625	638
Health assistance to the aged(b)	64	138	156	163	172	183
Total health	**29,400**	**32,355**	**34,986**	**36,194**	**37,763**	**39,657**
Social security and welfare						
Assistance to the aged(b)	24,834	27,173	28,460	30,170	31,847	33,720
Assistance to veterans and dependents	5,579	5,745	5,993	6,086	6,151	6,226
Assistance to people with disabilities	9,551	10,669	11,096	11,810	12,239	12,826
Assistance to families with children	19,595	24,489	24,463	25,493	26,584	27,513

Table A1: Estimates of expenses by function and sub-function (continued)

	Actuals	Estimates		Projections		
	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m	$m
Social security and welfare (continued)						
Assistance to the unemployed	5,565	5,428	5,701	5,733	6,078	6,293
Assistance to the sick	86	84	86	93	112	128
Assistance to the unemployed and the sick	*5,651*	*5,512*	*5,787*	*5,826*	*6,190*	*6,421*
Common youth allowance	2,235	2,247	2,318	2,391	2,442	2,513
Other welfare programmes	309	339	578	1,207	1,351	1,408
Aboriginal advancement nec	1,275	1,391	1,502	1,545	1,565	1,582
General administration	2,233	2,384	2,480	2,468	2,455	2,496
Total social security and welfare	**71,263**	**79,949**	**82,678**	**86,995**	**90,824**	**94,706**
Housing and community amenities						
Housing	1,381	1,227	1,240	1,246	1,263	1,286
Urban and regional development	113	142	174	142	107	102
Environment protection	268	284	257	259	254	233
Total housing and community amenities	**1,763**	**1,652**	**1,671**	**1,647**	**1,624**	**1,621**
Recreation and culture						
Broadcasting	1,030	1,108	1,152	1,164	1,151	1,166
Arts and cultural heritage	671	713	799	805	808	813
Sport and recreation	151	206	169	224	159	162
National estate and parks	210	206	222	224	223	211
Total recreation and culture	**2,062**	**2,233**	**2,342**	**2,417**	**2,341**	**2,352**
Fuel and energy	**3,395**	**3,692**	**3,922**	**4,001**	**3,914**	**4,036**
Agriculture, forestry and fishing						
Wool industry	76	57	58	61	61	61
Grains industry	115	127	131	135	135	135
Dairy industry	276	267	271	273	275	277
Cattle, sheep and pig industry	121	113	113	112	112	112
Fishing, horticulture and other agriculture	178	172	177	180	180	182
General assistance not allocated to specific industries	299	338	335	270	257	244
Rural assistance	224	513	675	196	112	54
Natural resources development	318	388	447	435	387	344
General administration	164	184	192	150	145	141
Total agriculture, forestry and fishing	**1,772**	**2,158**	**2,400**	**1,811**	**1,665**	**1,549**
Mining, manufacturing & construction	**1,502**	**1,717**	**1,830**	**1,791**	**1,705**	**1,705**
Transport and communication						
Communication	429	412	356	293	250	209
Rail transport(c)	17	451	3	28	6	0

Table A1: Estimates of expenses by function and sub-function (continued)

	Actuals	Estimates		Projections		
	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m	$m
Transport and communication (continued)						
Air transport	153	194	158	110	111	111
Road transport(c)	1,271	1,372	1,702	1,546	1,777	1,803
Sea transport	203	201	212	212	212	211
Other transport and communication	100	101	120	82	82	81
Total Transport and Communication	**2,174**	**2,731**	**2,550**	**2,273**	**2,437**	**2,414**
Other economic affairs						
Tourism and area promotion	156	142	175	174	163	165
Vocational and industry training	491	582	616	642	670	711
Labour market assistance to job seekers and industry	1,539	1,721	1,798	1,797	1,819	1,876
Industrial relations	270	271	291	305	307	309
Immigration	705	743	816	835	853	864
Total labour and employment affairs	*3,005*	*3,317*	*3,521*	*3,578*	*3,649*	*3,760*
Other economic affairs nec	642	782	816	803	795	804
Total other economic affairs	**3,803**	**4,241**	**4,512**	**4,556**	**4,607**	**4,730**
Other purposes						
Interest on Australian Government's behalf	4,602	3,995	3,881	3,618	3,548	3,593
Interest on behalf of States and Territories	27	19	11	1	0	0
Interest received on Australian Government stock	0	0	0	0	0	0
Public debt interest	*4,629*	*4,014*	*3,891*	*3,619*	*3,548*	*3,593*
Nominal superannuation interest	5,409	5,155	4,702	5,322	5,446	5,673
General revenue assistance - States and Territories	1,537	697	1,122	793	0	0
General capital assistance - States and Territories	0	0	0	0	0	0
Debt assistance(a)	0	37	54	196	0	0
Local government assistance	1,457	1,511	1,539	1,613	1,675	1,721
Revenue assistance to the States and Territories	166	156	160	164	168	172
Assistance to other governments	438	376	393	364	361	369
General purpose inter-government transactions	*3,598*	*2,775*	*3,269*	*3,129*	*2,204*	*2,262*
Natural disaster relief	95	144	97	97	97	91
Contingency reserve(d)	11	0	218	2,887	6,238	8,935
Total other purposes	**13,743**	**12,088**	**12,177**	**15,053**	**17,533**	**20,554**
Total expenses	**169,247**	**183,136**	**192,306**	**200,626**	**210,033**	**220,939**

(a) Debt redemption assistance expenses, paid by the Australian Office of Financial Management to the States and Territories under the *Financial Agreement Act 1994*, have been reclassified from the Financial and Fiscal Affairs Sub-function (General Public Services Function) to the Debt Assistance Sub-function (Other Purposes Function).

(b) The bulk of Department of Health and Ageing and Department of Veterans' Affairs expenses for assistance to the aged are now classified to the Assistance to the Aged sub-function (Social Security and Welfare Function).

(c) Splits of additional AusLink funding between road and rail from 2005-06 onwards are yet to be determined.

(d) Asset Sale related expenses are now treated as a component of the Contingency Reserve.

APPENDIX B: THE CONTINGENCY RESERVE

The Contingency Reserve (Other Purposes Function) is an allowance, included in aggregate expenses figuring, to reflect anticipated events that cannot be assigned to individual programmes in the preparation of the Australian Government budget estimates. The reserve is an estimating device used to ensure that the budget estimates are based on the best information available at the time of the Budget. It is not a general policy reserve.

While the reserve ensures that aggregate estimates are as close as possible to expected outcomes, it is not appropriated. Allowances that are included in the reserve can only be drawn upon once they have been appropriated by Parliament. These allowances are removed from the reserve and allocated to specific agencies for appropriation and for outcome reporting closer to the time when they eventuate.

The Contingency Reserve makes allowance in 2004-05 and the forward years for anticipated events including the following:

- an allowance for the tendency for estimates of expenses for existing government policy to be revised upwards in the forward years;
- an allowance for the tendency for the estimates of administered expenses for some specific agencies or functions to be overstated in the budget year;
- commercial-in-confidence and national security-in-confidence items that cannot be disclosed separately;
- decisions made too late for inclusion against individual agency estimates;
- the effect on the budget and forward estimates of economic parameter revisions received late in the process and hence not able to be allocated to individual agencies or functions;
  - An example of a late parameter revision is the estimated impact of the Australian Industrial Relations Commission’s Living Wage Case Decision released on 5 May 2004; and
- provision for events and pressures that are reasonably expected to affect the budget estimates.

The Contingency Reserve also includes expenses associated with the Government’s major asset sales and associated administration costs.

STATEMENT 7: BUDGET FUNDING

This statement discusses budget funding mechanisms and outlines the Government's intentions on issuance of debt instruments.

As announced in the 2003-04 Budget, the Government has decided to continue to issue Treasury bonds, despite the strong fiscal position, in order to support low cost interest rate risk management throughout the economy. Treasury bonds issuance will be tightly targeted to support the Treasury bond futures market — a key interest rate risk management market.

Late in 2003-04, issuance of a new 13-year Treasury bond (maturing in February 2017) will commence to support the 10-year bond futures contract. In addition, $600 million will be issued in August 2008 Treasury bonds in order to bring that bond line up to the size of other key benchmark lines.

In 2004-05, issuance of the February 2017 Treasury bond will continue. Issuance of a new 5-year Treasury bond will commence around the middle of the financial year.

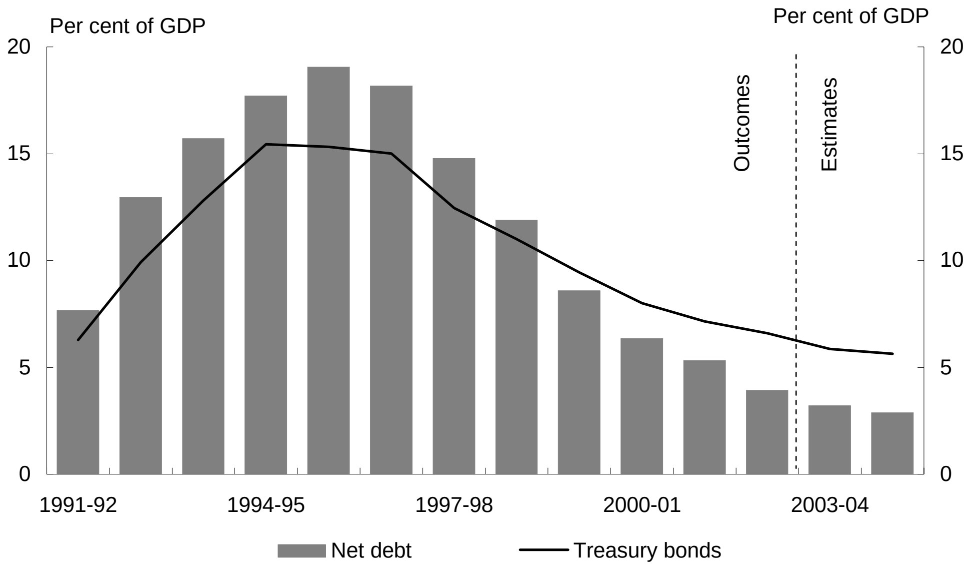
STATEMENT 7: BUDGET FUNDING

BACKGROUND

The Government's strong fiscal management since 1996 has significantly reduced Australian Government general government sector net debt. Net debt has fallen from a peak of 19.1 per cent of gross domestic product (GDP) or around $96 billion in 1995-96 to an estimated 3.2 per cent of GDP or around $26 billion in 2003-04. Net debt is expected to fall to 2.9 per cent of GDP or around $25 billion in 2004-05.

Reductions in gross debt outstanding have accompanied the fall in net debt. This is reflected principally in declining Commonwealth Government Securities (CGS) on issue. In particular, Treasury bonds on issue have fallen from around 15 per cent of GDP in 1995-96 to an expected 5.9 per cent of GDP in 2003-04 (Chart 1).

Chart 1: Australian Government general government sector net debt and Treasury bonds on issue[(a)]



(a) Treasury bonds on issue are net of Australian Government holdings and debt on issue for the States and Territories.
Source: Australian Bureau of Statistics Cat. No. 5513.0, Australian Government Final Budget Outcomes, Australian Office of Financial Management, and Treasury estimates.

As a result of the reduction in net debt, and concerns raised by key financial market stakeholders, the Australian Government undertook a public review of the CGS market in 2002. This review set out to determine whether there was a case for the Government to continue to issue debt despite a strong fiscal position.

The review concluded that closing the CGS market would lead to slightly higher interest rates, given the current state of development of Australian financial markets. This would result primarily from the higher costs associated with managing interest rate risk without a Treasury bond futures market. Further, the Australian financial markets may become less diversified and more vulnerable during periods of instability if the CGS market were eliminated. Accordingly, the Government announced in the 2003-04 Budget that it would maintain sufficient CGS on issue to support the Treasury bond futures market.

The outcome of the review means that the debt issuance programme is now tightly targeted at maintaining liquid and efficient CGS and Treasury bond futures markets. The outcome of the CGS review concluded Treasury bond outstandings of around $5 billion per line would be consistent with continued liquidity. In general terms, issuance of a long-dated bond will commence every second year to support the 10-year futures contract. Issuance of new mid-curve bond will commence in the year between commencement of new long-dated bonds, in order to provide better coverage of the short end of the yield curve.

As a result, around $5 billion of Treasury bond issuance will occur each year. However, because the current profile of Treasury bonds outstanding does not match the intended profile of outstandings, there will be a transition period to the new issuance strategy. During this transition period, which is expected to be two to three years, Treasury bond issuance may be slightly higher than $5 billion per year.

In addition, the issuance programme in any one year will be designed to focus mainly on the new bond that is being issued that year. While a total of $5 billion will be issued each year (once the transition period is complete), around three quarters of this issuance will be targeted at the new bond. That is, in the year that a new long-dated bond is commenced and the previous year's short-dated bond is being completed, priority will be given to bringing the new long-dated bond to a liquid level quickly.

DEBT ISSUANCE IN 2003-04

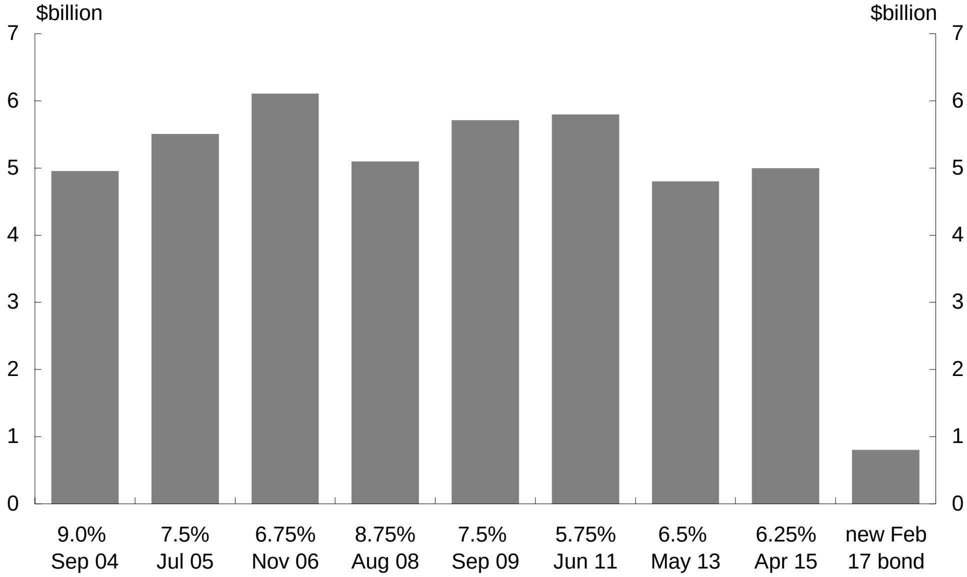
In the 2003-04 Budget, the Government announced its intention to issue between $2 billion and $3 billion of new Treasury bonds. To date, $1.5 billion of April 2015 Treasury bonds have been issued via five tenders this financial year. Taken with previous issues of April 2015 bonds, the total outstanding of April 2015 bonds is $4.7 billion. There is one further tender planned for this bond line in the remainder of this financial year. This tender will complete the issuance of this bond line.

A tender is planned to begin a new long-dated Treasury bond before 30 June 2004. In early June, the Australian Office of Financial Management will conduct the first tender of a new February 2017 Treasury bond. The initial tender will be between $800 million and $1 billion in size.

In order to ensure outstanding benchmark lines of Treasury bonds are all around $5 billion, an additional $600 million of Treasury bonds will be issued into the August 2008 Treasury bond line.

With the issuance outlined above, all benchmark Treasury bond lines (apart from the new February 2017 line) will have around $5 billion outstanding (Chart 2).

Chart 2: Benchmark Treasury bonds outstanding expected at 30 June 2004[(a)]



(a) Treasury bonds on issue are net of Australian Government holdings. Several smaller Treasury bond lines currently on issue, including the February 2006 and October 2007 Treasury bonds, are excluded from the chart as they are not considered benchmark bond lines.
Source: Australian Office of Financial Management.

Short-term deposits that the Australian Government holds with the Reserve Bank of Australia are mainly used to finance short-term imbalances between expenses and revenues. When there are insufficient short-term deposits, Treasury notes (which are a short-term debt instrument) are issued to assist with the Australian Government's within-year financing task. During 2003-04, there have been two Treasury note tenders totalling $1.1 billion. These Treasury notes matured in early November 2003. It is expected that term deposits will be sufficient to cover short term funding requirements for the remainder of 2003-04 so no further Treasury note tenders will be required.

During 2003-04, a total of around $5.4 billion in outstanding Treasury bonds (net of Australian Government holdings) is due to, or has, matured. Taking account of the total issuance outlined above, this means that there will be a net decrease in Treasury bonds outstanding of around $2 billion. As a result, the total stock of Treasury bonds outstanding (net of Australian Government holdings) will be around $48 billion at 30 June 2004. The reduction in Treasury bonds outstanding will be financed from the expected headline budget surplus and other financing transactions. The remaining surplus above this amount will be added to deposits at the Reserve Bank of Australia.

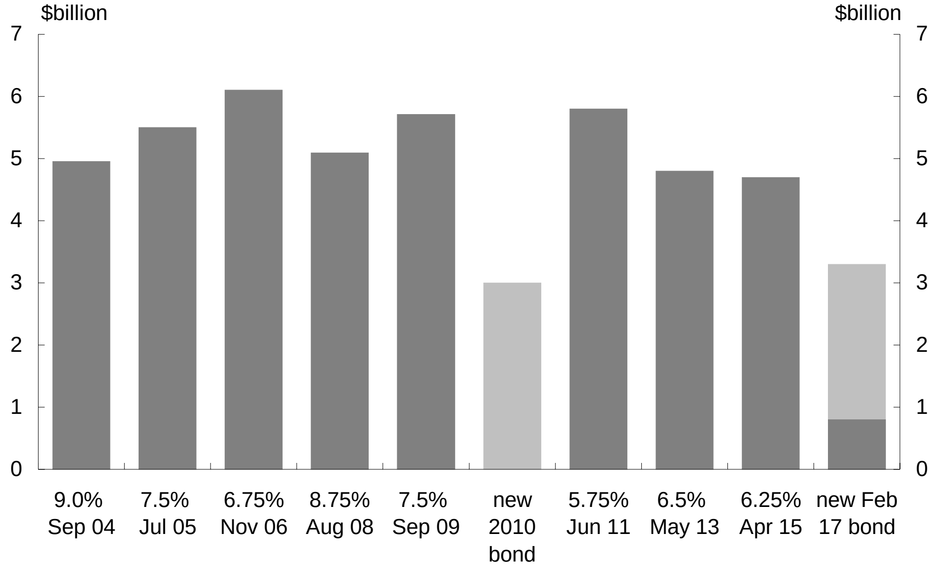
DEBT ISSUANCE IN 2004-05

Total issuance of Treasury bonds in 2004-05 is expected to be between $5 billion and $6 billion. In the early part of the financial year, issuance will be concentrated in the February 2017 Treasury bond, in order to bring that bond up to a liquid level of outstandings to facilitate trade in the 10-year futures contracts as early as possible. It is expected that around $2½ billion will be issued into the February 2017 line in 2004-05 to supplement the $800 million to $1 billion to be issued late in 2003-04. Further issuance of this line to bring it up to $5 billion outstanding will be undertaken in the first half of 2005-06.

Around the middle of the financial year a new 5-year Treasury bond will be issued. This bond will be required to support the ongoing efficient operation of the 3-year Treasury bond futures market. It is expected that around $3 billion of this new 5-year Treasury bond will be issued during 2004-05. The remaining issuance necessary to bring this line up to $5 billion outstandings will be undertaken in the first half of 2005-06.

During 2004-05, a total of around $5 billion in outstanding Treasury bonds (net of Australian Government holdings) is due to mature. Given the issuance outlined above and maturities during the year, the total stock of Treasury bonds outstanding (net of Australian Government holdings) will be between $48 billion and $49 billion at 30 June 2005. As Treasury bond issuance is likely to be equal to, or slightly larger than maturities, the entire amount of the expected headline budget surplus and other financing transactions will be added to deposits at the Reserve Bank of Australia.

Chart 3: Benchmark Treasury bonds outstanding expected at 30 June 2005(a)



(a) Treasury bonds on issue are net of Australian Government holdings. Several smaller Treasury bond lines currently on issue, including the February 2006 and October 2007 Treasury bonds, are excluded from the chart as they are not considered benchmark bond lines.
Note: The dark grey columns represent bonds outstanding at the beginning of the 2004-05 financial year. The light grey columns indicate new issuance in 2004-05.
Source: Australian Office of Financial Management and Treasury estimates.

Part 4
Financial Reporting Standards and Financial Statements

This part contains financial statements prepared in accordance with external reporting standards and discusses budget concepts. The external standards used in the budget are the Australian Bureau of Statistics accrual Government Finance Statistics framework and the Australian Accounting Standards.

This part includes reconciliation statements which explain how the two sets of financial statements compare.

This part also discusses a range of factors that pose a risk to the actual budget outcome in future years. These risks include changes in parameters, fiscal risks and contingent liabilities.

STATEMENT 8: FINANCIAL REPORTING STANDARDS AND BUDGET CONCEPTS

This statement describes the financial accounting frameworks relevant to the Australian Government.

STATEMENT 8: FINANCIAL REPORTING STANDARDS AND BUDGET CONCEPTS

The *Charter of Budget Honesty Act 1998* requires that the Budget be based on external reporting standards. Accordingly, the major external standards used in the Budget are the Australian Bureau of Statistics (ABS) accrual Government Finance Statistics (GFS) framework and Australian Accounting Standards, including Australian Accounting Standard No. 31 *Financial Reporting by Governments* (AAS31). The major fiscal aggregates (including the fiscal and underlying cash balances) are based on the accrual GFS framework.

The Charter also requires that departures from applicable external reporting standards be identified. These are disclosed in Appendix A to Statement 2 and Note 1 in Statement 10.

ACCRUAL GFS FRAMEWORK

The GFS reporting framework is a specialised financial reporting system designed to support economic analysis of the public sector. It allows comprehensive assessments to be made of the economic impact of government and is consistent with international statistical standards (the *System of National Accounts 1993* (SNA93) and the International Monetary Fund's (IMF) *Government Finance Statistics Manual 2001*).[1]

GFS financial statements are contained in Statements 2 and 9.

Nature of the GFS framework

The accrual GFS framework is based on an integrated recording of flows and stocks. Flows reflect the creation, transformation, exchange, transfer or extinction of economic value. They involve changes in the volume, composition or value of a unit's assets, liabilities and net worth. Stocks refer to a unit's holdings of assets, liabilities and net worth at a point in time.

The framework distinguishes between two types of flows: transactions and other economic flows.

- **Transactions** result from mutually agreed interactions between economic entities. Despite their compulsory nature, taxes are transactions deemed to occur by mutual agreement between the government and the taxpayer. Transactions that increase or

1 Additional information on the Australian accrual GFS framework is available in the ABS publication *Australian System of Government Finance Statistics: Concepts, Sources and Methods, 2003* (Cat. No. 5514.0.55.001).

decrease net worth (assets minus liabilities) are reported as revenue and expenses respectively in the operating statements[2].

- **Other economic flows** represent changes to the value of stocks that do not result from a transaction. Other economic flows arise from price movements (revaluations) and volume changes, including interest and exchange rate movements, and phenomena such as discoveries, depletion and destruction.

The GFS conceptual framework comprises a number of separate statements, each of which draws out analytical aggregates or balances of particular economic significance. Together, these aggregates provide for a thorough understanding of the financial position of the public sector. The GFS statements reported in the Budget are the operating statement, balance sheet, cash flow statement and statement of other economic flows.

Under the accrual GFS framework, flows are recorded in the period in which they occurred. As a result, prior period outcomes may be revised where information arises that could reasonably be expected to have been known in the past, is material in at least one of the effected periods and can be reliably assigned to the relevant period(s).

Operating statement

The operating statement presents details of transactions in GFS revenues, GFS expenses and the net acquisition of non-financial assets (net capital investment) for an accounting period.

GFS revenues arise from transactions that increase net worth and GFS expenses arise from transactions that decrease net worth. GFS revenues less GFS expenses gives the GFS net operating balance. The net operating balance is comparable to the National Accounts concept of government saving plus capital transfers.

The net acquisition of non-financial assets (net capital investment) measures the change in the Australian Government's stock of non-financial assets due to transactions. As such, it measures the net effect of purchases, sales and consumption (depreciation of fixed assets and use of inventory) of non-financial assets during an accounting period.

Net acquisition of non-financial assets equals gross fixed capital formation, less depreciation, plus changes (investment) in inventories, plus other transactions in non-financial assets.

---

2 Not all transactions impact on net worth. For example, transactions in financial assets and liabilities do not impact on net worth as they represent the swapping of assets and liabilities on the balance sheet.

- Gross fixed capital formation comprises purchases less sales of fixed assets (such as buildings) and net acquisitions of fixed assets under finance leases.

- Depreciation measures consumption of fixed assets, such as through physical deterioration or normal obsolescence, as they are used in production.

- Changes in inventories measures investment in new inventory stocks less use of current inventories.

- Other transactions in non-financial assets comprise mainly (for the Australian Government general government sector) changes in the value of work-in-progress and software assets, and transactions in non-reproducible, intangible assets (such as telecommunications spectrum).

Fiscal balance

The fiscal balance (or GFS net lending/borrowing) is the net operating balance less net capital investment. Thus, the fiscal balance includes the impact of net expenditure (effectively purchases less sales) on non-financial assets rather than consumption (depreciation) of non-financial assets.[3]

The fiscal balance measures the Australian Government's investment-saving balance. It measures in accrual terms the gap between government savings plus net capital transfers, and investment in non-financial assets. As such, it approximates the contribution of the Australian Government general government sector to the balance on the current account in the balance of payments.

A fiscal balance surplus indicates the Australian Government is lending to other sectors. A fiscal balance deficit indicates the Australian Government is using the financial resources of other sectors. Thus, fiscal balance can be viewed as a global indicator of the financial impact of Australian Government operations on the rest of the economy.

Balance sheet

The balance sheet shows stocks of assets, liabilities and GFS net worth. Net debt is also reported in the balance sheet.

Assets represent instruments or entities:

- over which ownership rights are enforced by an economic entity; and

3 The net operating balance includes consumption of non-financial assets because depreciation is a GFS expense. Depreciation also forms part of net capital investment, which (in the calculation of fiscal balance) offsets the inclusion of depreciation in the net operating balance.

- from which economic benefits may be derived by their owners from holding them or using them over a period of time.

Liabilities represent obligations to provide economic value to other institutional units.

Net debt

Net debt is the sum of selected financial liabilities (deposits held, advances received, government securities, loans, and other borrowing) less the sum of selected financial assets (cash and deposits; advances paid; and investments, loans and placements). Net debt does not include superannuation or superannuation related liabilities. Net debt is a common measure of the strength of a government's financial position. High levels of net debt impose a call on future revenue flows to service that debt.

Net interest payments is a concept related to net debt. Net interest payments is a cash measure defined as interest payments on gross debt less interest received. Net interest payments are affected by the volume of net debt on issue and by interest rates.

Net worth

The net worth of the general government sector is defined as assets less liabilities. Apart from the effect of revaluations (recorded in the statement of other economic flows), changes in general government sector net worth reflect the net operating balance. For the public financial corporations and public non-financial corporations sectors, net worth is defined as assets less liabilities less shares and other contributed capital. Net worth is an economic measure of wealth, reflecting the contribution of the Australian Government to the wealth of Australia.

The net worth measure is a more comprehensive indicator of a government's overall financial position than net debt as it incorporates a government's non-financial assets, such as land and other fixed assets, as well as certain financial assets and liabilities not captured by the net debt measure, most notably accrued employee superannuation liabilities. For example, a limitation of the net debt measure is that the sale of physical assets decreases net debt, with proceeds from sales increasing financial assets. Net worth recognises this increase in financial assets is funded by a decrease in physical assets. Net worth itself, however, also has limitations. It can be volatile, some non-financial assets can be difficult to measure, and changes can reflect circumstances beyond the direct control of the Government.

Cash flow statement

The cash flow statement identifies how cash is generated and applied in a single accounting period. Cash means cash on hand (notes and coins held and deposits held at call with a bank or other financial institution) and cash equivalents (highly liquid investments that are readily convertible to cash on hand at the investor's option and overdrafts considered integral to the cash management function).

The cash flow statement reflects a cash basis of recording (rather than an accrual basis) where information is derived indirectly from underlying accrual transactions and movements in balances. This, in effect, means that transactions are captured when cash is received or when cash payments are made. Cash transactions are identified specifically because cash management is considered an integral function of accrual budgeting.

Underlying cash balance

The underlying cash balance (GFS surplus/deficit) is the cash counterpart of the fiscal balance, reflecting the Australian Government's cash investment-saving balance. The underlying cash balance measure is conceptually equivalent under the current accrual framework and the previous cash framework. For the general government sector, the underlying cash balance is calculated as shown below.

Net cash flows from operating activities

plus

Net cash flows from investments in non-financial assets

less

Net acquisitions of assets acquired under finance leases and similar arrangements[4]

equals

Underlying cash balance

An underlying cash surplus reflects the extent to which cash is available to the Australian Government to either increase its financial assets or decrease its liabilities (assuming no revaluations and other changes occur). An underlying cash deficit measures the extent to which the Australian Government requires cash, either by running down its financial assets or drawing on other sectors' cash reserves.

Headline cash balance

The headline cash balance is calculated by adding net cash flows from investments in financial assets for policy purposes to the underlying cash balance.

Cash flows from investments in financial assets for policy purposes include equity transactions and net advances.[5] Equity transactions include equity injections into controlled businesses and privatisations of government businesses. Net advances

4 The underlying cash balance treats the acquisition and disposal of non-financial assets in the same manner regardless of whether they occur by purchase/sale or finance lease — acquisitions reduce the underlying cash balance and disposals increase the underlying cash balance. However, finance leases do not generate cash flows at the time of acquisition or disposal equivalent to the value of the asset. As such, net acquisitions of assets under finance leases are not shown in the body of the cash flow statement but are reported as a supplementary item for the calculation of the underlying cash balance.

5 Cash flows from investments in financial assets for policy purposes were called net advances under the cash budgeting framework.

include net loans to the States, net loans to students under the Higher Education Contribution Scheme (HECS) and contributions to international organisations that increase the Australian Government's financial assets.

Statement of other economic flows (reconciliation of net worth)

The statement of other economic flows outlines changes in net worth driven by economic flows other than GFS revenues and GFS expenses. Accordingly, the GFS system includes a fourth financial statement that presents changes in net worth in an accounting period due to other economic flows (the effect of transactions is reported in the operating statement). Other economic flows, GFS revenues and GFS expenses sum to the total change in net worth during a period. [6]

Other economic flows are changes in the value of assets or liabilities due to price movements or volume changes. Most other economic flows for the Australian Government general government sector arise from price movements in its assets and liabilities, including:

- changes in the value of investments in commercial entities, including through changes in share prices;
- writedowns in asset values, such as through greater allowances for bad and doubtful debts;
- changes in the valuation of superannuation and employee compensation liabilities due to economic and demographic changes; and
- valuation changes due to movements in foreign exchange rates and interest rates.

The Australian Government also has a small number of volume changes, including assets recognised for the first time and changes to assets and liabilities flowing from reclassifications and accounting policy changes.

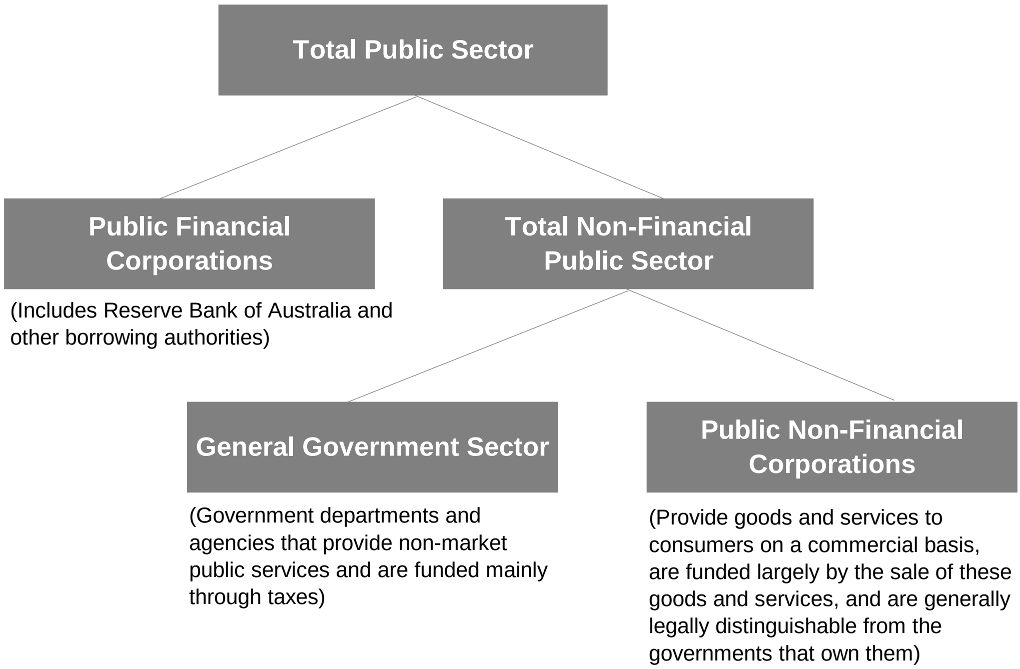
---

6 The ABS publication *Australian System of Government Finance Statistics: Concepts, Sources and Methods, 2003* (Cat. No. 5514.0.55.001) calls the statement of other economic flows the 'Statement of Stocks and Flows'.

Sectoral classifications

To assist in analysing the public sector, GFS data are presented by institutional sector. GFS distinguishes between the general government sector, the public non-financial corporations sector and the public financial corporations sector, as shown in Figure 1.

Figure 1: Institutional structure of the public sector



Budget reporting focuses on the general government sector. The general government sector provides public services that are mainly non-market in nature and for the collective consumption of the community, or involve the transfer or redistribution of income. These services are largely financed through taxes and other compulsory levies, although user charging and external funding have increased in recent years. This sector comprises all government departments, offices and some other bodies.

The public non-financial corporations sector comprises bodies that provide goods and services that are mainly market, non-regulatory and non-financial in nature, and are financed predominantly through sales to the consumers of these goods and services. In general, public non-financial corporations are legally distinguishable from the governments that own them. Australian Government public non-financial corporations include Telstra, Australia Post and the Australian Government Solicitor.

Together the general government sector and the public non-financial corporations sector comprise the non-financial public sector.

The GFS coverage of the public sector also includes public financial corporations. Public financial corporations are public sector bodies that engage in financial intermediation services or auxiliary financial services and are able to incur financial liabilities on their own account (such as taking deposits, issuing securities or providing insurance services). This sector includes the Reserve Bank of Australia, the Export Finance and Insurance Corporation and Medibank Private. Information on public financial corporations is not included in the budget papers as public financial corporations undertake financial intermediation, which is a fundamentally different function from that performed by other public entities. Under the Uniform Presentation Framework, public financial corporations information is only required to be reported in budget outcome statements.

The total public sector comprises all sectors of government — general government, the public non-financial corporations sector and the public financial corporations sector.

AUSTRALIAN ACCOUNTING STANDARD NO. 31 (AAS31) REPORTING FRAMEWORK

Australian Accounting Standard No. 31 *Financial Reporting by Governments* requires governments to prepare accrual-based general purpose financial reports in relation to the assets they control and any liabilities incurred, their revenues and expenses, and cash flows. Reporting under this framework is intended to provide a consolidated overview of the financial performance, position and cash flows of government, including in the area of financing and investing activities.

There are three main general purpose statements that must be prepared in accordance with the AAS31 framework. These are:

- a statement of financial performance, which includes an operating result;
- a statement of financial position, which shows net assets; and
- a statement of cash flows, which includes net increase/decrease in cash held.

In addition to these general purpose statements, the standard requires notes to the financial statements to be prepared which report disaggregated information in relation to the financial performance and financial position of the government. The notes should also include other information seen as relevant to users.

While AAS31 provides a general framework for accrual budgeting and financial reporting by governments, compliance with all other applicable accounting standards is required. Exceptions to this rule are explicitly stated in AAS31.

A full set of AAS31 financial statements and accompanying notes prepared for the general government sector are contained in Statement 10.

RECONCILIATION OF GFS AND AAS31 AGGREGATES

There is a general consistency of treatment of the elements of financial statements between GFS and accounting standards. Both frameworks are based on the concept of economic events that give rise to stocks and flows. As a result, the definitions of stocks are broadly similar under the two frameworks and relate to the control of economic benefits, while flows are defined with reference to changes in stocks.

The GFS and AAS31 definitions of the scope of the public sector agree in almost all cases, with AAS31 recommending the same segmentation of the public sector into general government, public non-financial corporations and public financial corporations sectors.

Transactions are generally treated in a similar manner by GFS and accounting standards; however, where GFS is a framework designed to facilitate macro-economic analysis, AAS31 is designed as a standard for general purpose financial reporting. The different objectives of the two systems lead to some variation in the treatment of certain items. This differing treatment relates predominantly to the definitions of revenues and expenses under the two frameworks.

In particular, revaluations of assets and liabilities are classified differently under the AAS31 and GFS standards. Major revaluations include writedowns of bad and doubtful debts (excluding those that are mutually agreed), changes in the valuation of superannuation liabilities, and gains and losses due to changes in foreign exchange rates and interest rates.

Under AAS31 reporting, valuation changes generally affect revenues or expenses and therefore the operating result. However, under GFS reporting, revaluations are not considered to be transactions (that is, they are considered to be other economic flows) and accordingly do not form part of revenues or expenses. Therefore, most revaluations are not taken into account in the calculation of the GFS net operating balance or fiscal balance. However, revaluations still impact on GFS assets and liabilities, as can be seen in the statement of other economic flows.

Some of the major differences between the GFS and AAS31 treatments of transactions are outlined in Table 1. Further information on the differences between the two systems is provided in the ABS publication *Australian System of Government Finance Statistics: Concepts, Sources and Methods, 2003* (Cat. No. 5514.0.55.001).

Table 1: Selected differences between AAS31 and GFS reporting standards

Issue	AAS31 Treatment	GFS Treatment
Asset writedowns	Treated as part of operating expenses.	Treated as revaluations (other economic flows), except for mutually agreed writedowns, and therefore not included in expenses.
Gains and losses on assets	Treated as part of operating revenues/expenses.	Treated as revaluations (other economic flows) and therefore not included in revenues/expenses.
Provisions for bad and doubtful debts	Treated as part of operating expenses and included in the balance sheet as an offset to assets.	Act of creating provisions is not considered an economic event and is therefore not considered an expense or included in the balance sheet. The Australian Government departs from this latter requirement (see Appendix A to Statement 2).
Interest flows related to swaps and other financial derivatives	Treated as operating revenues and expenses.	Treated as other economic flows and so not included in revenues and expenses.
Acquisition of defence weapons platforms	Treated as capital expenditure. Defence weapons platforms appear as an asset on the balance sheet. Depreciation expense on assets is recorded in the operating statement.	Treated as an expense at the time of acquisition. Defence weapons platforms do not appear as an asset on the balance sheet and no depreciation is recorded in the operating statement.
Valuation of assets and liabilities	Classes of assets and liabilities are measured using a range of methods. The predominant methods for valuing different asset classes include historic cost and market value.	Individual assets and liabilities are measured at current market value based on current market prices or a suitable proxy where market prices are not available.
Finance leases	Treats finance leases as if an asset were purchased from borrowings. That is, the lease payment is split into an interest component (which is shown as an operating expense) and a principal component. The asset and the liability are recorded on the balance sheet. This convention does not apply to the cash flow statement, which does not record the acquisition of the asset or the liability.	As per the accounting standard, except that the GFS cash flow statement includes the acquisition of the asset as a supplementary item for the calculation of the surplus/deficit (underlying cash balance).

Following the broad strategic direction of the Financial Reporting Council, the Australian Accounting Standards Board is currently pursuing harmonisation of GFS and Australian accounting standards. A converged financial reporting framework will reduce confusion associated with the publication of two sets of financial statements and increase the accessibility of government budget and outcome reports.

Table 2 reconciles GFS revenue and expenses with their AAS31 counterparts.

Table 2: Reconciliation of GFS and AAS31 revenue and expenses

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
GFS revenue (Statement 9)	**220,372**	**228,341**	**238,753**	**251,729**	**264,839**
less GST revenue for States and Territories	34,175	35,190	37,370	39,530	41,710
GFS revenue (Statement 2)	**186,197**	**193,151**	**201,383**	**212,199**	**223,129**
plus asset revenue recognised for the first time	182	1	3	3	1
plus foreign exchange gains	306	0	0	0	0
plus other economic revaluations	222	49	20	20	20
plus proceeds from the sale of assets	1,580	915	746	11,857	11,855
plus swap interest revenue	1,909	2,191	2,262	2,113	1,707
AAS31 revenue (Statement 10)	**190,396**	**196,308**	**204,414**	**226,191**	**236,712**
GFS expenses (Statement 9)	**216,456**	**226,846**	**237,316**	**248,843**	**261,884**
less GST grants to States and Territories	33,240	34,460	36,610	38,720	40,850
less GST mutually agreed writedowns	80	80	80	90	95
GFS expenses (Statement 2)	**183,136**	**192,306**	**200,626**	**210,033**	**220,939**
plus actuarial revaluations	-840	0	0	0	0
plus net writedown of assets/bad and doubtful debts	2,567	1,447	1,508	1,622	1,727
plus foreign exchange losses	0	0	0	0	0
plus other economic adjustments	5	0	0	0	0
plus value of assets sold	1,080	808	712	2,214	2,206
plus swap interest expense	1,570	2,031	2,093	1,940	1,548
plus defence weapons platforms depreciation	2,729	2,367	2,029	2,098	2,167
less defence weapons platforms investment	2,556	2,869	3,027	3,309	3,653
plus AusAid IDA/ADF expenses	0	573	0	0	296
AAS31 expenses (Statement 10)	**187,689**	**196,663**	**203,940**	**214,598**	**225,230**

Table 3 reconciles the accounting operating result to the GFS net operating balance and the fiscal balance (GFS net lending).

The AAS31 net operating result is equal to the AAS31 revenues less expenses. Similarly, GFS revenues less expenses equal the GFS net operating balance. Consequently, the reconciliation between the AAS31 operating result before extraordinary items and the GFS net operating balance relates directly to differences in the definitions of revenues and expenses which are shown in Table 2.

The second part of the Table 3 reconciliation shows the adjustment for net capital investment required to derive the fiscal balance from the GFS net operating balance.

As discussed previously, the fiscal balance is calculated as the net operating balance less net capital investment. This is a useful economic indicator as it represents the gap between government saving (less capital transfers) and investment, and so is included at the end of the GFS operating statement. In AAS31, there is no equivalent measure to the fiscal balance. That is, the AAS31 statement of financial performance stops at the operating result and includes no information on net capital investment.

Table 3: Reconciliation of AAS31 net operating result and fiscal balance

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
AAS31 operating result before extraordinary items (Statement 10)	**2,707**	**-355**	**474**	**11,594**	**11,481**
Net differences from revenue and expense definitions	1,209	1,851	964	-8,707	-8,527
GFS net operating balance (Statement 9)	**3,916**	**1,496**	**1,438**	**2,887**	**2,955**
less purchase of property, plant and equipment and intangibles	5,206	5,723	5,725	5,829	6,012
less assets acquired under finance leases	-3	7	7	29	4
less other non-financial assets	-25	71	187	-11	-55
less increase in inventories	106	-42	-69	21	4
plus defence weapons platforms investment	2,556	2,869	3,027	3,309	3,653
plus proceeds from sales of property, plant and equipment and intangibles	1,118	810	647	489	487
plus depreciation and amortisation	4,322	4,300	4,159	4,293	4,421
less weapons depreciation	2,729	2,367	2,029	2,098	2,167
Fiscal balance (GFS net lending) (Statement 9)(a)	**3,899**	**1,348**	**1,392**	**3,011**	**3,384**
Impact of GST	-855	-650	-680	-720	-765
Fiscal balance (GFS net lending) (Statement 2)(a)	**3,044**	**698**	**712**	**2,291**	**2,619**

(a) The fiscal balance estimates in Statement 9 are higher than those presented in Statement 2, as explained in the introduction to Statement 9.

STATEMENT 9: GOVERNMENT FINANCE STATISTICS STATEMENTS

The financial tables presented in this statement are prepared in accordance with the Australian Bureau of Statistics (ABS) accrual Government Finance Statistics (GFS) framework.

The Australian, State and Territory Governments have an agreed framework — the Accrual Uniform Presentation Framework — for the presentation of government financial information on a basis consistent with the ABS GFS publication. This statement presents Australian Government data on an ABS GFS basis, as required by the Uniform Presentation Framework, except for the departures (other than in relation to the treatment of goods and services tax (GST)) detailed in Attachment A to Statement 2.

In accordance with Uniform Presentation Framework requirements, this statement also contains an update of the Australian Government's Loan Council Allocation.

STATEMENT 9: GOVERNMENT FINANCE STATISTICS STATEMENTS

Financial tables presented in this statement are prepared in accordance with the Australian Bureau of Statistics (ABS) accrual Government Finance Statistics (GFS) framework.

The tables include an operating statement, balance sheet and cash flow statement for the Australian Government general government, public non-financial corporations and total non-financial public sectors. A statement of other economic flows is also included for the Australian Government general government sector.

The Australian, State and Territory Governments have an agreed framework — the Accrual Uniform Presentation Framework — for the presentation of government financial information on a basis consistent with the ABS GFS publication. This statement presents Australian Government data on an ABS GFS basis, as required by the Uniform Presentation Framework, except for the departures (other than in relation to the treatment of goods and services tax (GST)) detailed in Attachment A to Statement 2.

The only difference between the Australian Government general government sector statements in Statement 2 and this statement is the treatment of the GST. Under the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations*, GST is collected by the Australian Taxation Office, as an agent for the States and Territories, and appropriated to the States and Territories. Consequently, it is not shown as Australian Government revenue in other parts of this document. However, the tables in this statement show GST as taxation revenue and payments to the States as grant expenses.

As a result of the different treatments of GST related transactions, the fiscal balance, net operating balance and net worth estimates in this statement differ from those reported elsewhere in this document. This accounting difference is an accrual issue only: it represents the effect of GST revenue accrued but not yet received and, therefore, not yet paid or payable to the States (as GST obligations to the States are on a cash basis).[1] The underlying cash balance is not affected and provides identical results under both treatments of GST receipts.

Consistent with ABS practice, transactions between the Australian Government general government and public non-financial corporations sectors are included in the tables produced for these sectors, but are removed from the total non-financial public sector tables as they are transactions internal to that sector.

1 Table 3 in Statement 8 shows the difference in the net operating and fiscal balance estimates resulting from the two treatments. The change in expenses when moving between the two GFS presentations of the estimates is less than the change in revenue.

Statement 8 provides reconciliations between key GFS aggregates and their Australian Accounting Standard No. 31 counterparts.

GOVERNMENT FINANCE STATISTICS STATEMENTS

Table 1: Australian Government general government sector operating statement

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
GFS revenue					
Taxation revenue	208,257	217,770	227,747	240,095	252,852
Current grants and subsidies	0	0	0	0	0
Sales of goods and services	4,192	4,266	4,404	4,537	4,615
Interest income	1,244	1,082	1,049	1,682	2,556
Dividend income	4,171	2,570	2,879	2,756	2,144
Other	2,507	2,653	2,675	2,660	2,672
Total GFS revenue	**220,372**	**228,341**	**238,753**	**251,729**	**264,839**
GFS expenses					
Gross operating expenses					
Depreciation	1,593	1,933	2,130	2,195	2,254
Superannuation	1,946	2,213	2,162	2,101	2,160
Salaries and wages	11,989	12,011	12,408	12,705	12,833
Payment for supply of goods and services	40,014	43,330	44,282	46,302	48,941
Other operating expenses	2,312	2,443	2,419	2,418	2,412
Total gross operating expenses	*57,854*	*61,929*	*63,400*	*65,720*	*68,600*
Nominal superannuation interest expense	5,155	4,702	5,322	5,446	5,673
Other interest expenses	4,248	4,121	3,844	3,773	3,816
Other property expenses	0	0	0	0	0
Current transfers					
Grant expenses	67,874	71,543	74,482	77,522	81,165
Subsidy expenses	5,643	6,064	6,260	6,362	6,571
Personal benefit payments in cash	72,511	74,986	80,687	86,446	92,401
Other current transfers	0	0	0	0	0
Total current transfers	*146,028*	*152,593*	*161,429*	*170,330*	*180,137*
Capital transfers	3,171	3,501	3,320	3,575	3,657
Total GFS expenses	**216,456**	**226,846**	**237,316**	**248,843**	**261,884**
Net operating balance(a)	**3,916**	**1,496**	**1,438**	**2,887**	**2,955**
Net acquisition of non-financial assets					
Purchases of non-financial assets	2,618	2,856	2,705	2,549	2,363
less Sales of non-financial assets	879	727	642	484	484
less Depreciation	1,593	1,933	2,130	2,195	2,254
plus Change in inventories	106	-42	-69	21	4
plus Other movements in non-financial assets	-235	-6	182	-16	-58
Total net acquisition of non-financial assets	**18**	**148**	**45**	**-125**	**-429**
Net lending/fiscal balance(a)(b)	**3,899**	**1,348**	**1,392**	**3,011**	**3,384**

(a) The fiscal balance and net operating balance estimates in this table differ from those presented elsewhere in the Budget reflecting the treatment of the GST as an Australian Government tax.
(b) The term fiscal balance is not used by the ABS.

Table 2: Australian Government general government sector balance sheet

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
GFS assets					
Financial assets					
Cash and deposits	1,607	1,553	1,492	1,315	982
Advances paid	19,027	20,408	21,440	22,824	24,587
Investments, loans and placements(a)	19,668	8,756	8,722	8,717	8,759
Other non-equity assets	19,448	20,204	21,520	23,524	25,618
Equity(b)	47,061	47,636	47,632	39,555	28,275
Total financial assets	106,812	98,556	100,807	95,935	88,221
Non-financial assets					
Land	4,576	4,410	4,410	4,491	4,536
Buildings (excluding heritage)	13,417	13,377	13,483	13,535	13,589
Plant, equipment and infrastructure(c)	7,951	8,227	8,348	8,236	7,932
Inventories	4,237	4,195	4,126	4,146	4,150
Heritage and cultural assets(c)	4,949	4,950	4,953	4,956	4,957
Other non-financial assets	1,714	1,842	1,812	1,726	1,623
Total non-financial assets	*36,844*	*37,000*	*37,131*	*37,090*	*36,788*
Total GFS assets	**143,656**	**135,556**	**137,938**	**133,025**	**125,009**
GFS liabilities					
Deposits held	325	325	325	325	325
Advances received	0	0	0	0	0
Government securities(a)	60,555	49,894	48,637	35,159	21,050
Loans	5,271	5,055	4,882	4,717	4,593
Other borrowing	175	138	100	89	54
Superannuation liability	87,869	89,007	92,157	95,226	98,545
Other employee entitlements and provisions	8,426	8,338	8,457	8,592	8,716
Other non-equity liabilities	23,031	23,670	23,912	24,583	25,825
Total GFS liabilities	**185,652**	**176,428**	**178,470**	**168,692**	**159,109**
Net worth(d)(e)	**-41,996**	**-40,872**	**-40,532**	**-35,666**	**-34,100**
Net financial worth(f)	-78,840	-77,872	-77,663	-72,756	-70,888
Net debt(g)	26,024	24,696	22,289	7,435	-8,306

(a) For 2004-05 and the forward years, transactions relating to debt management activities in *Assets — Investments, Loans and Placements* and *Liabilities — Government Securities* have been netted. This treatment has been applied because of the uncertainty associated with the actual split between government securities and financial assets acquired for debt management purposes.

(b) Equity includes the valuation of the Telstra shareholding, which is valued at the average of the daily share price over a 90-day period, except in the sale years where the valuation is based on the expected sale price.

(c) *Heritage and cultural assets* were previously included in *Plant, equipment and infrastructure*.

(d) The net worth estimates in this table differ from those presented elsewhere in the Budget reflecting the treatment of GST as an Australian Government tax.

(e) Net worth is calculated as total assets minus total liabilities.

(f) Net financial worth equals total financial assets minus total liabilities. That is, it excludes non-financial assets.

(g) Net debt equals the sum of deposits held, advances received, government securities, loans and other borrowing, minus the sum of cash and deposits, advances paid, and investments, loans and placements.

Table 3: Australian Government general government sector cash flow statement[(a)]

	2003-04 $m	2004-05 $m	2005-06 $m	2006-07 $m	2007-08 $m
Cash receipts from operating activities					
Taxes received(b)	203,789	214,122	224,090	236,101	248,714
Receipts from sales of goods and services(c)	4,169	4,256	4,403	4,525	4,610
Grants and subsidies received	0	0	0	0	0
Interest receipts	1,132	1,014	838	1,357	2,197
Dividends	3,207	3,214	3,199	2,756	2,144
GST input credits received by general government(c)	0	0	0	0	0
Other receipts	2,417	2,455	2,459	2,432	2,426
Total receipts	**214,714**	**225,062**	**234,989**	**247,170**	**260,091**
Cash payments for operating activities					
Payments for goods and services(c)	-41,542	-44,576	-45,427	-47,539	-50,206
Grants and subsidies paid(d)	-75,033	-79,235	-82,650	-85,996	-89,816
Interest paid	-4,113	-3,888	-4,658	-3,917	-3,598
Personal benefit payments	-70,694	-75,246	-80,625	-86,007	-91,778
Salaries, wages and other entitlements	-16,768	-16,593	-16,602	-17,182	-17,367
GST payments by general government to taxation authority(c)	0	0	0	0	0
Other payments for operating activities	-499	-1,013	-1,194	-1,041	-1,004
Total payments	**-208,649**	**-220,550**	**-231,156**	**-241,683**	**-253,769**
Net cash flows from operating activities	**6,065**	**4,511**	**3,833**	**5,487**	**6,322**
Cash flows from investments in non-financial assets					
Sales of non-financial assets	1,112	804	647	489	487
Purchases of new and secondhand non-financial assets	-2,594	-2,917	-2,887	-2,509	-2,304
Net cash flows from investments in non-financial assets	**-1,482**	**-2,113**	**-2,240**	**-2,020**	**-1,817**
Net cash flows from investments in financial assets for policy purposes	**-599**	**-1,374**	**-1,560**	**9,395**	**9,230**
Cash flows from investments in financial assets for liquidity purposes					
Increase in investments	-70	-41	10	31	-21
Net cash flows from investments in financial assets for liquidity purposes	**-70**	**-41**	**10**	**31**	**-21**
Cash flows from financing activities					
Advances received (net)	0	0	0	0	0
Borrowing (net)	-1,697	315	-514	-13,548	-14,226
Deposits received (net)	-1	0	0	0	0
Other financing (net)	-2,948	-1,352	409	477	179
Net cash flows from financing activities	**-4,645**	**-1,037**	**-105**	**-13,071**	**-14,047**
Net increase/decrease in cash held	**-731**	**-54**	**-61**	**-177**	**-333**
Net cash from operating activities and investments in non-financial assets	**4,583**	**2,398**	**1,594**	**3,468**	**4,505**
Finance leases and similar arrangements(e)	3	-7	-7	-29	-4
Equals surplus(+)/deficit(-)	**4,586**	**2,391**	**1,587**	**3,438**	**4,501**

(a) A positive number denotes a cash inflow; a negative sign denotes a cash outflow.
(b) Includes GST cash receipts on an Australian Government tax basis, which are $5 million greater in 2003-04 than GST cash receipts measured by the Australian Government on a State tax basis (as shown in Statement 10, Note 16).
(c) GST flows are excluded from these categories.
(d) Includes GST cash payments on an Australian Government tax basis.
(e) The acquisition of assets under finance leases decreases the surplus or increases the deficit. The disposal of assets previously held under finance leases increases the surplus or decreases the deficit.

Table 4: Australian Government general government sector statement of other economic flows (reconciliation of net worth)

	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Opening net worth	**-49,524**	**-41,996**	**-40,872**	**-40,532**	**-35,666**
Opening net worth adjustments(a)	**-891**	**0**	**0**	**0**	**0**
Adjusted opening net worth	**-50,415**	**-41,996**	**-40,872**	**-40,532**	**-35,666**
Change in net worth from operating transactions	**3,916**	**1,496**	**1,438**	**2,887**	**2,955**
Change in net worth from other economic flows					
Revaluation of equity(b)	3,210	637	34	3,253	19
Net writedowns of assets (including bad and doubtful debts)(c)	-2,414	-1,582	-1,658	-1,787	-1,907
Assets recognised for the first time(c)	-1	1	3	3	1
Defence weapon platform adjustment(c)	0	0	0	0	0
Liabilities recognised for the first time	0	0	0	0	0
Actuarial revaluations	840	0	0	0	0
Net foreign exchange gains	306	0	0	0	0
Net swap interest received	339	160	168	173	159
Market valuation of debt	1,809	454	304	222	209
Other economic revaluations(c)(d)	412	-42	50	115	130
Total other economic flows	**4,502**	**-371**	**-1,098**	**1,979**	**-1,388**
Closing net worth	**-41,996**	**-40,872**	**-40,532**	**-35,666**	**-34,100**

(a) Includes the initial recognition of a provision for asbestos related claims. At the time of the *2002-03 Final Budget Outcome* a reliable actuarial measure was not available. Following an actuarial review a provision for asbestos-related claims was included in the audited *2002-03 Consolidated Financial Statements*. This liability has now been back dated to 2002-03.

(b) Revaluations of equity reflects changes in the market valuation of commercial entities, including a change in the value of the Telstra shareholding which is valued at the average of the daily share price over a 90-day period, except in the sale years where the valuation is based on the expected sale price. This line also reflects any equity revaluations at the point of disposal or sale.

(c) Defence weapons are treated as expenses rather than assets under the GFS framework, hence, changes in value do not contribute to net worth and are not included in other economic flows. The adjustment to remove defence weapons has now been reallocated to net writedown of assets, assets recognised for the first time and other economic revaluations.

(d) Largely reflects revaluation of assets and liabilities.

Table 5: Australian Government public non-financial corporations operating statement

	2003-04 $m	2004-05 $m
GFS revenue		
Current grants and subsidies	241	177
Sales of goods and services	24,547	25,489
Interest income	77	79
Other	28	13
Total GFS revenue	**24,893**	**25,757**
GFS expenses		
Gross operating expenses		
Depreciation	3,525	3,477
Salaries, wages and other entitlements	5,131	5,258
Other operating expenses	10,952	10,509
Total gross operating expenses	*19,608*	*19,244*
Interest expenses	590	508
Other property expenses	1,912	1,512
Current transfers		
Tax expenses	1,677	2,075
Other current transfers	0	0
Total current transfers	*1,677*	*2,075*
Capital transfers	0	0
Total GFS expenses	**23,787**	**23,338**
Net operating balance	**1,106**	**2,419**
Net acquisition of non-financial assets		
Purchases of non-financial assets	3,303	3,361
less Sales of non-financial assets	363	48
less Depreciation	3,525	3,477
plus Change in inventories	-47	35
plus Other movements in non-financial assets	-12	14
Total net acquisition of non-financial assets	**-645**	**-116**
Net lending/fiscal balance(a)	**1,752**	**2,535**

(a) The term fiscal balance is not used by the ABS.

Table 6: Australian Government public non-financial corporations balance sheet

	2003-04 $m	2004-05 $m
GFS assets		
Financial assets		
Cash and deposits	1,649	1,821
Advances paid	0	0
Investments, loans and placements	680	678
Other non-equity assets	4,947	5,174
Equity	350	350
Total financial assets	*7,625*	*8,023*
Non-financial assets		
Land and fixed assets	26,563	26,234
Other non-financial assets(a)	699	699
Total non-financial assets	*27,262*	*26,933*
Total GFS assets	**34,887**	**34,957**
GFS liabilities		
Deposits held	0	0
Advances received	0	0
Borrowing	11,216	9,616
Unfunded superannuation liability and other employee entitlements	1,868	1,892
Provisions (other than depreciation and bad and doubtful debts)(a)	3,012	2,956
Other non-equity liabilities	1,111	1,018
Total GFS liabilities	**17,206**	**15,482**
Shares and other contributed capital	**62,168**	**62,613**
Net worth(b)	**-44,487**	**-43,138**
Net financial worth(c)	-71,749	-70,072
Net debt(d)	8,887	7,117

(a) Includes the elimination of commercial taxation adjustments for future income tax benefits and deferred income tax.
(b) Net worth is calculated as total assets minus total liabilities minus shares and other contributed capital. The negative net worth recorded for this sector reflects a higher valuation of listed Australian Government corporations by the sharemarket than the value of net assets recorded by these corporations.
(c) Net financial worth equals total financial assets minus total liabilities minus shares and other contributed capital. That is, it excludes non-financial assets.
(d) Net debt equals the sum of deposits held, advances received and borrowing, minus the sum of cash and deposits, advances paid, and investments, loans and placements.

Table 7: Australian Government public non-financial corporations cash flow statement[(a)]

	2003-04 $m	2004-05 $m
Cash receipts from operating activities		
Receipts from sales of goods and services	24,540	25,440
Grants and subsidies received	241	177
GST input credit receipts	15	17
Other receipts	160	49
Total receipts	**24,956**	**25,683**
Cash payments for operating activities		
Payment for goods and services	-6,882	-7,230
Interest paid	-468	-419
Salaries, wages and other entitlements	-5,248	-5,269
GST payments to taxation authority	-1,338	-1,308
Other payments for operating activities(b)	-4,957	-4,421
Total payments	**-18,893**	**-18,647**
Net cash flows from operating activities	**6,063**	**7,037**
Cash flows from investments in non-financial assets		
Sales of non-financial assets	397	48
Purchases of new and secondhand non-financial assets	-3,348	-3,361
Net cash flows from investments in non-financial assets	**-2,952**	**-3,313**
Net cash flows from investments in financial assets for policy purposes	**0**	**0**
Cash flows from investments in financial assets for liquidity purposes		
Increase in investments	-131	-3
Net cash flows from investments in financial assets for liquidity purposes	**-131**	**-3**
Cash flows from financing activities		
Advances received (net)	0	0
Borrowing (net)	-905	-1,543
Deposits received (net)	0	0
Distributions paid (net)(c)	-1,912	-1,512
Other financing (net)	234	-522
Net cash flows from financing activities	**-2,583**	**-3,578**
Net increase/decrease in cash held	**398**	**143**
Net cash from operating activities and investments in non-financial assets	**3,111**	**3,724**
Finance leases and similar arrangements(d)	0	0
Distributions paid(c)	-1,912	-1,512
Equals surplus(+)/deficit(-)	**1,199**	**2,212**

(a) A positive number denotes a cash inflow; a negative sign denotes a cash outflow.
(b) Other payments for operating activities includes distributions paid to the general government sector from public non-financial corporations.
(c) Distributions paid comprise public non-financial corporations dividends to non-general government shareholders.
(d) The acquisition of assets under finance leases decreases the surplus or increases the deficit. The disposal of assets previously held under finance leases increases the surplus or decreases the deficit.

Table 8: Australian Government total non-financial public sector operating statement

	2003-04 $m	2004-05 $m
GFS revenue		
Taxation revenue	206,580	215,695
Current grants and subsidies	0	0
Sales of goods and services	28,186	29,223
Interest income	1,321	1,161
Dividend income	1,979	1,012
Other	2,536	2,666
Total GFS revenue	**240,602**	**249,757**
GFS expenses		
Gross operating expenses		
Depreciation	5,118	5,410
Superannuation	1,962	2,228
Salaries and wages	17,120	17,269
Payment for supply of goods and services	47,942	51,472
Other operating expenses	2,575	2,704
Total gross operating expenses	*74,717*	*79,083*
Nominal superannuation interest expense	5,155	4,702
Other interest expenses	4,838	4,628
Other property expenses	1,912	1,512
Current transfers		
Grant expenses	67,874	71,543
Subsidy expenses	5,401	5,887
Personal benefit payments in cash	72,511	74,986
Other current transfers	0	0
Total current transfers	*145,787*	*152,416*
Capital transfers	3,171	3,501
Total GFS expenses	**235,579**	**245,842**
Net operating balance(a)	**5,023**	**3,915**
Net acquisition of non-financial assets		
Purchases of non-financial assets	5,920	6,175
less Sales of non-financial assets	1,241	734
less Depreciation	5,118	5,410
plus Change in inventories	59	-7
plus Other movements in non-financial assets	-247	8
Total net acquisition of non-financial assets	**-627**	**32**
Net lending/fiscal balance(a)(b)	**5,650**	**3,883**

(a) The fiscal balance and net operating balance estimates in this table differ from those presented elsewhere in the Budget reflecting the treatment of the GST as an Australian Government tax.
(b) The term fiscal balance is not used by the ABS.

Table 9: Australian Government total non-financial public sector balance sheet

	2003-04 $m	2004-05 $m
GFS assets		
Financial assets		
Cash and deposits	3,256	3,374
Advances paid	19,027	20,408
Investments, loans and placements	20,347	9,434
Other non-equity assets	24,388	25,370
Equity	14,472	14,601
Total financial assets	*81,490*	*73,188*
Non-financial assets		
Land and fixed assets	63,163	62,919
Other non-financial assets	943	1,014
Total non-financial assets	*64,106*	*63,933*
Total GFS assets	**145,596**	**137,121**
GFS liabilities		
Deposits held	325	325
Advances received	0	0
Government securities	60,555	49,894
Loans	5,271	5,055
Other borrowing	11,390	9,754
Unfunded superannuation liability and other employee entitlements	98,163	99,237
Other provisions	6,102	6,035
Other non-equity liabilities	21,044	21,601
Total GFS liabilities	**202,851**	**191,903**
Shares and other contributed capital	**29,228**	**29,228**
Net worth(a)(b)	**-86,483**	**-84,010**
Net financial worth(b)(c)	-150,590	-147,943
Net debt(d)	34,911	31,813

(a) Net worth is calculated as total assets minus total liabilities minus shares and other contributed capital. The negative net worth recorded for this sector partly reflects a higher valuation of listed Australian Government corporations by the sharemarket than the value of net assets recorded by these corporations.

(b) Net worth and net financial worth for the non-financial public sector now equal the sum of the general government and public non-financial corporations sectors. This is due to the elimination of commercial taxation adjustments for future income tax benefits and deferred income tax now being made within the public non-financial corporations sector.

(c) Net financial worth equals total financial assets minus total liabilities minus shares and other contributed capital. That is, it excludes non-financial assets.

(d) Net debt equals the sum of deposits held, advances received, government securities, loans and other borrowing, minus the sum of cash and deposits, advances paid, and investments, loans and placements.

Table 10: Australian Government total non-financial public sector cash flow statement(a)

	2003-04 $m	2004-05 $m
Cash receipts from operating activities		
Taxes received	202,111	212,047
Receipts from sales of goods and services(b)	26,197	27,267
Grants and subsidies received	0	0
Interest receipts	1,132	1,014
Dividends	1,246	1,668
GST input credit receipts(b)	0	0
Other receipts	2,608	2,505
Total receipts	**233,295**	**244,501**
Cash payments for operating activities		
Payments for goods and services(b)	-47,266	-50,667
Grants and subsidies paid	-74,791	-79,058
Interest paid	-4,580	-4,306
Personal benefit payments	-70,694	-75,246
Salaries, wages and other entitlements	-22,016	-21,862
GST payments to taxation authority(b)	0	0
Other payments for operating activities	-1,818	-1,814
Total payments	**-221,167**	**-232,953**
Net cash flows from operating activities	**12,128**	**11,548**
Cash flows from investments in non-financial assets		
Sales of non-financial assets	1,509	852
Purchases of new and secondhand non-financial assets	-5,943	-6,279
Net cash flows from investments in non-financial assets	**-4,434**	**-5,426**
Net cash flows from investments in financial assets for policy purposes	**-599**	**-1,374**
Cash flows from investments in financial assets for liquidity purposes		
Increase in investments	-201	-44
Net cash flows from investments in financial assets for liquidity purposes	**-201**	**-44**
Cash flows from financing activities		
Advances received (net)	0	0
Borrowing (net)	-2,601	-1,228
Deposits received (net)	-1	0
Distributions paid (net)(c)	-1,912	-1,512
Other financing (net)	-2,714	-1,875
Net cash flows from financing activities	**-7,228**	**-4,615**
Net increase/decrease in cash held	**-333**	**89**
Net cash from operating activities and investments in non-financial assets	**7,694**	**6,122**
Finance leases and similar arrangements(d)	3	-7
Distributions paid(c)	-1,912	-1,512
Equals surplus(+)/deficit(-)	**5,785**	**4,603**

(a) A positive number denotes a cash inflow; a negative sign denotes a cash outflow.
(b) GST flows are excluded from these categories.
(c) *Distributions paid* comprise public non-financial corporations dividends to non-general government shareholders.
(d) The acquisition of assets under finance leases decreases the surplus or increases the deficit. The disposal of assets previously held under finance leases increases the surplus or decreases the deficit.

Table 11: Australian Government general government sector taxation revenue by source

	2003-04 $m	2004-05 $m
Taxes on income, profits and capital gains		
Income and capital gains levied on individuals	98,690	104,080
Income and capital gains levied on enterprises	43,020	46,020
Income taxes levied on non-residents	0	0
Total taxes on income, profits and capital gains	**141,710**	**150,100**
Taxes on employers' payroll and labour force	3,491	3,516
Taxes on property	13	14
Taxes on the provision of goods and services		
Sales/goods and services tax	35,165	36,180
Excises and levies	21,602	21,906
Taxes on international trade	5,585	5,335
Other	0	0
Total taxes on the provision of goods and services	**62,353**	**63,421**
Taxes on use of goods and performance of activities	690	718
Total GFS taxation revenue	**208,257**	**217,770**

Table 12: Australian Government purchases of non-financial assets by function

	Estimates		Projections		
	2003-04 $m	2004-05 $m	2005-06 $m	2006-07 $m	2007-08 $m
General public services	495	694	463	553	533
Defence	484	609	888	828	812
Public order and safety	274	275	196	-13	147
Education	19	16	16	16	15
Health	95	105	87	72	74
Social security and welfare	175	226	111	184	135
Housing and community amenities	455	452	530	474	448
Recreation and culture	269	185	359	67	218
Fuel and energy	4	3	5	-1	2
Agriculture, forestry and fishing	16	10	14	0	17
Mining, manufacturing and construction	45	15	46	6	21
Transport and communications	67	52	53	468	38
Other economic affairs	182	213	230	155	173
Other purposes	38	3	-291	-261	-271
General government purchases of non-financial assets	**2,618**	**2,856**	**2,705**	**2,549**	**2,363**

APPENDIX A: LOAN COUNCIL ALLOCATION

Under Loan Council arrangements, every year the Australian Government and each State and Territory nominate a Loan Council Allocation. A jurisdiction's Loan Council Allocation incorporates:

- the estimated non-financial public sector underlying cash balance (made up from the general government and public non-financial corporations sector balances);
- net cash flows from investments in financial assets for policy purposes; and
- memorandum items, which involve transactions that are not formally borrowings but nevertheless have many of the characteristics of borrowings.

Loan Council Allocation nominations are considered by the Loan Council, having regard to each jurisdiction's fiscal position and reasonable infrastructure requirements, as well as the macroeconomic implications of the aggregate figure.

As set out in Table 13, the Australian Government's 2004-05 Loan Council Allocation Budget update is a $2,277 million surplus. This compares with the Australian Government's nominated, and Loan Council endorsed, Loan Council Allocation surplus of $3,749 million.

The Australian Government has no plans in 2004-05 for any public infrastructure projects with private sector involvement that require disclosure under present arrangements.

Table 13: Australian Government Loan Council Allocation Budget update for 2004-05

	2004-05 Nomination $m	2004-05 Budget Estimate $m
General government sector cash deficit(+)/surplus(-)	-3,829	-2,391
Public non-financial corporations sector cash deficit(+)/surplus(-)	-1,412	-2,212
Non-financial public sector cash deficit(+)/surplus(-)	-5,241	-4,603
less Net cash flows from investments		
in financial assets for policy purposes(a)	-968	-1,374
plus Memorandum items(b)	524	951
Loan Council Allocation	**-3,749**	**-2,277**

(a) Such transactions involve the transfer or exchange of a financial asset and are not included within the cash deficit/surplus. However, the cash flow from investments in financial assets for policy purposes has implications for a government's call on financial markets.

(b) For the Australian Government, memorandum items comprise the change in net present value (NPV) of operating leases (with NPV greater than $5 million), university borrowings, over-funding of superannuation and an adjustment to exclude the net financing requirements of statutory marketing authorities and Telstra from the Loan Council Allocation.

STATEMENT 10: AUSTRALIAN ACCOUNTING STANDARDS FINANCIAL STATEMENTS

This statement provides financial tables prepared on an accrual basis in accordance with applicable Australian Accounting Standards, including Australian Accounting Standard No. 31 *Financial Reporting by Governments* (AAS31), except where departures from the standard are identified in Note 1.

A reconciliation between the Australian Government's general government AAS31 and Government Finance Statistics (GFS) revenue, expenses and operating results is provided in Statement 8.

STATEMENT 10: AUSTRALIAN ACCOUNTING STANDARDS FINANCIAL STATEMENTS

Table 1: Statement of financial performance for the Australian Government general government sector — AAS31

	Note	Estimates		Projections		
		2003-04	2004-05	2005-06	2006-07	2007-08
		$m	$m	$m	$m	$m
Revenues						
Taxation						
Income taxation	3	141,710	150,100	157,740	167,520	177,580
Indirect taxation	4	27,515	27,545	27,609	27,943	28,411
Fringe benefits tax		3,180	3,190	3,220	3,310	3,410
Other taxes		1,575	1,642	1,704	1,689	1,639
Total taxation revenue		**173,980**	**182,477**	**190,273**	**200,462**	**211,040**
Non-taxation						
Sales of goods and services		4,294	4,369	4,507	4,640	4,717
Interest and dividends	5	7,324	5,844	6,190	6,550	6,407
Net foreign exchange gains		306	0	0	0	0
Proceeds from the sale of assets		1,580	915	746	11,857	11,855
Other sources of non-taxation revenue	6	2,911	2,703	2,698	2,682	2,693
Total non-taxation revenue		**16,416**	**13,831**	**14,141**	**25,729**	**25,672**
Total revenue		**190,396**	**196,308**	**204,414**	**226,191**	**236,712**
Expenses						
Goods and services						
Employees	7	20,463	21,368	22,311	22,669	23,078
Suppliers	8	14,642	16,099	15,295	15,593	16,210
Depreciation and amortisation	9	4,322	4,300	4,159	4,293	4,421
Net writedown of assets		2,985	1,881	1,957	2,072	2,205
Net foreign exchange losses		0	0	0	0	0
Value of assets sold		1,084	813	714	2,399	2,381
Other goods and services expenses		7,076	7,533	7,879	8,201	8,592
Total goods and services		**50,572**	**51,994**	**52,316**	**55,228**	**56,887**
Subsidies benefits and grants						
Personal benefits		85,108	88,713	95,247	101,679	108,631
Subsidies		9,947	10,386	10,987	11,360	11,900
Grants	10	36,189	39,378	39,426	40,602	42,441
Total subsidies benefits and grants		**131,243**	**138,477**	**145,660**	**153,640**	**162,973**
Borrowing costs						
Interest		5,850	6,170	5,943	5,708	5,350
Other borrowing costs		24	22	21	21	21
Total interest and other borrowing costs		**5,874**	**6,192**	**5,965**	**5,729**	**5,371**
Total expenses		**187,689**	**196,663**	**203,940**	**214,598**	**225,230**
Operating result		**2,707**	**-355**	**474**	**11,594**	**11,481**
Extraordinary items		0	0	0	0	0
Operating result after extraordinary items		**2,707**	**-355**	**474**	**11,594**	**11,481**

Table 2: Statement of financial position for the Australian Government general government sector — AAS31

	Note	Estimates		Projections		
		2003-04	2004-05	2005-06	2006-07	2007-08
		$m	$m	$m	$m	$m
Assets						
Financial assets						
Cash		1,607	1,553	1,492	1,315	982
Receivables		30,341	31,960	33,872	36,796	39,846
Investments	11	35,942	25,075	25,064	23,385	21,767
Equity accounted investments		451	451	451	451	451
Accrued revenue		374	347	353	392	438
Other financial assets		24	24	25	25	26
Total financial assets		**68,740**	**59,410**	**61,259**	**62,365**	**63,509**
Non-financial assets	12					
Land and buildings (excluding heritage)		17,993	17,786	17,893	18,026	18,125
Infrastructure(a)		38,974	39,652	40,671	41,670	42,752
Heritage and cultural assets(a)		4,949	4,950	4,953	4,956	4,957
Intangibles		1,470	1,527	1,513	1,444	1,397
Inventories		4,237	4,195	4,126	4,146	4,150
Other non-financial assets		1,787	1,460	1,443	1,420	1,364
Total non-financial assets		**69,410**	**69,570**	**70,598**	**71,662**	**72,746**
Total assets		**138,150**	**128,979**	**131,857**	**134,027**	**136,255**
Liabilities						
Debt						
Government securities	11	55,359	45,019	44,684	31,303	17,206
Loans		4,202	3,972	3,794	3,626	3,498
Leases		151	116	80	70	36
Deposits		325	325	325	325	325
Overdrafts		0	0	0	0	0
Other debt		1,094	1,106	1,110	1,112	1,116
Total debt		**61,131**	**50,539**	**49,993**	**36,437**	**22,181**
Provisions and payables						
Employees and superannuation	13	96,295	97,346	100,614	103,818	107,262
Suppliers		2,244	2,262	2,242	2,256	2,267
Personal benefits payable		5,010	4,860	4,954	5,417	6,072
Subsidies payable		373	344	267	240	238
Grants payable	14	9,004	9,816	10,003	10,204	10,768
Other provisions and payables		9,225	9,392	8,860	9,042	9,261
Total provisions and payables		**122,152**	**124,019**	**126,940**	**130,976**	**135,869**
Total liabilities		**183,283**	**174,558**	**176,932**	**167,413**	**158,049**
Net assets	15	**-45,133**	**-45,579**	**-45,075**	**-33,386**	**-21,794**
Equity						
Accumulated results		-78,624	-78,759	-78,311	-65,076	-51,963
Reserves		33,491	33,180	33,236	31,690	30,169
Capital		0	0	0	0	0
Total equity		**-45,133**	**-45,579**	**-45,075**	**-33,386**	**-21,794**

(a) Heritage and cultural assets were previously included in infrastructure.

Table 3: Statement of cash flows for the Australian Government general government sector — AAS31

	Note	Estimates		Projections		
		2003-04	2004-05	2005-06	2006-07	2007-08
		$m	$m	$m	$m	$m
Operating activities						
Cash received						
Taxation	16	170,442	179,561	187,376	197,279	207,761
Sales of goods and services		4,443	4,536	4,682	4,806	4,892
Interest		3,042	3,138	3,086	3,500	3,994
Dividends		3,207	3,214	3,199	2,756	2,144
GST input credit receipts		2,461	2,653	2,629	2,714	2,841
Other		2,471	2,504	2,479	2,452	2,446
Total operating cash received		**186,066**	**195,606**	**203,451**	**213,507**	**224,078**
Cash used						
Payments to employees		18,480	18,868	19,030	19,457	19,627
Payments to suppliers		17,391	18,752	17,916	18,371	19,121
Subsidies paid		9,423	9,849	10,454	10,814	11,341
Personal benefits		83,291	88,973	95,185	101,239	108,008
Grant payments		35,681	38,164	39,231	40,395	41,873
Interest and other financing costs		5,870	6,126	6,794	5,847	5,491
GST payments to taxation authority		129	131	132	138	141
Other		7,146	7,570	7,844	8,182	8,570
Total operating cash used		**177,410**	**188,433**	**196,587**	**204,443**	**214,171**
Net cash from operating activities		**8,656**	**7,173**	**6,864**	**9,063**	**9,907**
Investing activities						
Cash received						
Proceeds from asset sales program		376	0	0	11,280	11,280
Proceeds from sales of property, plant and equipment and intangibles		1,142	810	647	489	487
Net loans, advances and HECS		0	0	0	0	0
Other net investing cash received		343	106	102	88	88
Total investing cash received		**1,860**	**915**	**750**	**11,857**	**11,855**
Cash used						
Purchase of property, plant and equipment and intangibles		5,187	5,792	5,915	5,818	5,957
Net loans, advances and HECS		752	1,192	1,405	1,717	1,877
Other net investing cash paid	11	406	147	91	242	285
Total investing cash used		**6,344**	**7,131**	**7,411**	**7,776**	**8,118**
Net cash from investing activities		**-4,484**	**-6,216**	**-6,662**	**4,081**	**3,737**
Financing activities						
Cash received						
Net cash received from currency issues		0	0	0	0	0
Other		0	0	294	266	287
Total financing cash received		**0**	**0**	**294**	**266**	**287**
Cash used						
Net repayments of borrowings	11	1,697	-315	514	13,548	14,226
Other		3,206	1,327	43	39	39
Total financing cash used		**4,903**	**1,012**	**557**	**13,587**	**14,265**
Net cash from financing activities		**-4,903**	**-1,012**	**-263**	**-13,321**	**-13,978**
Net increase/decrease in cash held	2	**-731**	**-54**	**-61**	**-177**	**-333**

NOTES TO THE AAS31 FINANCIAL STATEMENTS

Note 1: External reporting standards

The *Charter of Budget Honesty Act 1998* requires that the budget be based on external reporting standards and that departures from applicable external reporting standards be identified.

The financial statements included in this statement have been prepared on an accrual basis in accordance with applicable Australian Accounting Standards, including Australian Accounting Standard No. 31 *Financial Reporting by Governments* (AAS31).

AAS31 requires governments to prepare accrual-based general purpose financial reports. This means that assets, liabilities, revenues and expenses are recorded in financial statements when they have their economic impact on the government, rather than when the cash flow associated with these transactions occurs. Consistent with AAS31, a statement of financial performance, a statement of financial position and a statement of cash flows have been prepared for the budget year and the three forward years.

The accounting policies in this statement are generally consistent with the accounting policies in AAS31. While the scope for financial reporting recommended in AAS31 is the whole of government (that is, the Australian Government public sector), in accordance with the *Charter of Budget Honesty Act 1998*, the budget presentation of financial estimates covers the general government sector only.

AAS31 and other relevant accounting standards would suggest the gross amount of goods and services tax (GST) be included in the Australian Government's financial statements. However, under the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations*, GST is collected by the Australian Taxation Office as an agent for the States and Territories, and appropriated to the States and Territories. Therefore, accrued GST revenues and associated payments to the States and Territories are not recorded in the financial statements.

Note 2: Reconciliation of cash

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Operating result (revenues less expenses)	**2,707**	**-355**	**474**	**11,594**	**11,481**
less **Revenues not providing cash**					
Foreign exchange gains	306	0	0	0	0
Gains from asset sales programme	267	0	0	9,436	9,454
Gains from sale of assets	234	107	34	21	20
Other	473	285	336	455	471
Total revenues not providing cash	**1,281**	**392**	**371**	**9,912**	**9,945**
plus **Expenses not requiring cash**					
Increase/(decrease) in employee entitlements	1,983	2,494	3,268	3,204	3,444
Depreciation/amortisation expense	4,322	4,300	4,159	4,293	4,421
Provision for bad and doubtful debts	624	466	542	641	727
Provision for diminution in value of assets	391	136	118	139	120
Losses from asset sales programme	0	0	0	0	0
Losses from sale of assets	0	0	0	0	0
Foreign exchange losses	0	0	0	0	0
Other	-56	-26	-11	-10	-23
Total expenses not requiring cash	**7,264**	**7,371**	**8,076**	**8,266**	**8,690**
plus **Cash provided by working capital items**					
Decrease in inventories	0	42	69	0	0
Decrease in receivables	0	0	0	0	0
Decrease in other financial assets	57	0	0	0	0
Decrease in other non-financial assets	146	398	0	6	1
Increase in benefits subsidies and grants payable	2,350	821	290	670	1,224
Increase in suppliers' liabilities	0	16	0	14	12
Increase in other provisions and payables	0	55	0	0	0
Total cash provided by working capital items	**2,553**	**1,332**	**359**	**690**	**1,236**
less **Cash used by working capital items**					
Increase in inventories	88	0	0	20	4
Increase in receivables	2,111	595	750	1,407	1,441
Increase in other financial assets	0	8	58	23	1
Increase in other non-financial assets	0	0	0	0	0
Decrease in benefits subsidies and grants payable	41	179	76	28	1
Decrease in other provisions and payables	275	0	772	96	108
Decrease in suppliers' liabilities	73	0	18	0	0
Total cash used by working capital items	**2,588**	**783**	**1,675**	**1,575**	**1,555**
equals *Net cash from/(to) operating activities*	8,656	7,173	6,864	9,063	9,907
Net cash from/(to) investing activities	-4,484	-6,216	-6,662	4,081	3,737
Net cash from operating activities and investment	**4,172**	**957**	**202**	**13,144**	**13,644**
Net cash from/(to) financing activities	-4,903	-1,012	-263	-13,321	-13,978
equals Net (decrease)/increase in cash	**-731**	**-54**	**-61**	**-177**	**-333**

Note 2(a): Consolidated Revenue Fund

The estimated and projected cash balances reflected in the statement of financial position for the Australian Government general government sector (Table 2) include the reported cash balances controlled and administered by Australian Government agencies subject to the *Financial Management and Accountability Act 1997* and the reported cash balances controlled and administered by entities, subject to the *Commonwealth Authorities and Companies Act 1997* (CAC Act), that implement public policy through the provision of primarily non-market services.

Revenues or monies raised by the Executive Government automatically form part of the Consolidated Revenue Fund by force of section 81 of the Australian Constitution. For practical purposes, total Australian Government general government sector cash, less cash controlled and administered by CAC Act entities, plus special public monies, represents the Consolidated Revenue Fund referred to in section 81 of the Australian Constitution. On this basis, the balance of the Consolidated Revenue Fund is shown below.

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Total general government sector cash (Statement 10)	1,607	1,553	1,492	1,315	982
less CAC Agency cash balances	814	748	786	731	678
plus Special public monies	74	74	76	80	84
Balance of Consolidated Revenue Fund at 30 June	**867**	**879**	**782**	**664**	**388**

Further information on the Consolidated Revenue Fund is included in Budget Paper No. 4, *Agency Resourcing 2004-05.*

Note 3: Income taxation revenue — accrual AAS31

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Individuals and other witholding tax					
Gross income tax withholding	89,870	95,150	100,280	107,220	114,490
Gross other individuals	19,760	20,390	20,940	21,510	22,510
less Refunds	12,200	12,850	13,490	14,220	15,140
Total individuals and other witholding tax	97,430	102,690	107,730	114,510	121,860
Companies	37,310	39,400	42,230	44,760	47,300
Superannuation funds					
Contributions and earnings	4,510	5,520	5,290	5,630	6,040
Superannuation surcharge	1,260	1,390	1,410	1,330	1,190
Total superannuation funds	5,770	6,910	6,700	6,960	7,230
Petroleum resource rent tax	1,200	1,100	1,080	1,290	1,190
Total income taxation revenue	**141,710**	**150,100**	**157,740**	**167,520**	**177,580**

Note 4: Indirect taxation revenue — accrual AAS31

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Excise duty					
Petroleum and other fuel products	13,160	13,320	13,460	13,650	13,760
Crude oil	310	320	300	290	280
Other excise	7,470	7,580	7,650	7,770	7,870
Total excise duty revenue	20,940	21,220	21,410	21,710	21,910
Customs duty revenue	5,585	5,335	5,149	5,113	5,321
Other indirect tax revenue	990	990	1,050	1,120	1,180
GST	34,175	35,190	37,370	39,530	41,710
less transfers to States and Territories in relation to GST revenue	34,175	35,190	37,370	39,530	41,710
GST revenue	0	0	0	0	0
Mirror taxes	312	331	348	365	384
less transfers to States and Territories in relation to mirror tax revenue	312	331	348	365	384
Mirror tax revenue	0	0	0	0	0
Indirect taxation revenue	**27,515**	**27,545**	**27,609**	**27,943**	**28,411**

Note 5: Interest and dividend revenue

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Interest					
Interest from other governments					
State and Territory debt	38	28	17	15	14
Housing agreements	178	174	170	166	162
Total interest from other governments	**215**	**202**	**187**	**181**	**176**
Interest from other sources					
Swap interest	1,909	2,191	2,262	2,113	1,707
Advances	19	20	20	20	20
Deposits	3	3	3	3	3
Bills receivable	6	6	6	6	6
Bank deposits	172	192	196	198	198
Indexation of HECS receivable and other student loans	276	272	307	422	438
Other	553	387	329	851	1,714
Total interest from other sources	**2,938**	**3,071**	**3,124**	**3,613**	**4,087**
Total interest	**3,153**	**3,273**	**3,311**	**3,795**	**4,263**
Dividends					
Dividends from associated entities	4,126	2,543	2,847	2,701	2,104
Other dividends	45	27	33	55	40
Total dividends	**4,171**	**2,570**	**2,879**	**2,756**	**2,144**
Total interest and dividends	**7,324**	**5,844**	**6,190**	**6,550**	**6,407**

Note 6: Other sources of non-taxation revenue

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Industry contributions	125	121	111	105	100
International Monetary Fund related revenue	35	29	29	29	29
Other	2,752	2,553	2,557	2,548	2,563
Total other sources of non-taxation revenue	**2,911**	**2,703**	**2,698**	**2,682**	**2,693**

Note 7: Employees expenses

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Salaries and wages(a)	11,989	12,011	12,408	12,705	12,833
Leave and other entitlements	1,486	1,531	1,552	1,558	1,570
Separations and redundancies	72	72	82	82	82
Workers compensation premiums	0	0	0	0	0
Other (including superannuation)	6,916	7,755	8,269	8,325	8,592
Total employee expenses	**20,463**	**21,368**	**22,311**	**22,669**	**23,078**

(a) Salaries and wages do not include superannuation.

Note 8: Suppliers expenses

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Supply of goods and services	12,953	14,279	13,474	13,744	14,340
Operating lease rental expenses	1,559	1,540	1,570	1,592	1,610
Other	131	279	252	257	260
Total suppliers	**14,642**	**16,099**	**15,295**	**15,593**	**16,210**

Note 9: Depreciation and amortisation expenses

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Depreciation					
Specialist military equipment	2,729	2,367	2,029	2,098	2,167
Buildings	537	509	590	600	601
Heritage and cultural assets	40	41	42	42	42
Other infrastructure, plant and equipment	712	1,029	1,122	1,151	1,198
Total depreciation	**4,019**	**3,947**	**3,782**	**3,890**	**4,008**
Total amortisation	**303**	**354**	**377**	**403**	**413**
Total depreciation and amortisation	**4,322**	**4,300**	**4,159**	**4,293**	**4,421**

Note 10: Grants expenses

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
State and Territory governments	23,592	25,435	25,921	26,942	28,132
Non-profit organisations	1,675	1,650	1,695	1,720	1,749
Overseas	276	1,032	349	275	673
Private sector	1,923	1,593	1,435	1,114	1,061
Local governments	362	305	354	355	353
Other	8,361	9,363	9,672	10,196	10,472
Total grants	**36,189**	**39,378**	**39,426**	**40,602**	**42,441**

Note 11: Government securities

For 2004-05 and the forward years, transactions relating to debt management activities have been netted in the statement of financial position and cash flows. In the statement of financial position, the *financial assets — investments* category excludes financial assets acquired for debt management purposes, while the *debt — government securities* category is shown net of financial assets acquired for debt management purposes. In the statement of cash flows, the *investing activities — cash used/received — other* categories exclude cash used to acquire/redeem financial assets for debt management purposes, while the *financing activities — cash used — net repayments of borrowings* category is shown net of these amounts.

This netting treatment has been applied because of the uncertainty associated with the actual split between government securities and financial assets acquired for debt management purposes.

Note 12: Total non-financial assets

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Land and buildings					
Land	4,576	4,410	4,410	4,491	4,536
Buildings	13,417	13,377	13,483	13,535	13,589
Total land and buildings	**17,993**	**17,786**	**17,893**	**18,026**	**18,125**
Infrastructure					
Specialist military equipment	31,023	31,425	32,323	33,434	34,820
Other	7,951	8,227	8,348	8,236	7,932
Total infrastructure	**38,974**	**39,652**	**40,671**	**41,670**	**42,752**
Intangibles					
Computer software	1,388	1,473	1,482	1,436	1,410
Other	82	54	31	8	-13
Total intangibles	**1,470**	**1,527**	**1,513**	**1,444**	**1,397**
Heritage and cultural assets	4,949	4,950	4,953	4,956	4,957
Total heritage and cultural assets	**4,949**	**4,950**	**4,953**	**4,956**	**4,957**
Inventories	4,237	4,195	4,126	4,146	4,150
Total inventories	**4,237**	**4,195**	**4,126**	**4,146**	**4,150**
Other non-financial assets					
Prepayments	1,543	1,145	1,144	1,138	1,137
Other	244	315	299	282	227
Total other non-financial assets	**1,787**	**1,460**	**1,443**	**1,420**	**1,364**
Total non-financial assets	**69,410**	**69,570**	**70,598**	**71,662**	**72,746**

Note 13: Employee and superannuation liabilities

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Superannuation	87,869	89,007	92,157	95,226	98,545
Leave and other entitlements	4,173	4,245	4,117	4,119	4,122
Accrued salaries and wages	339	95	230	228	207
Workers compensation claims	1,437	1,432	1,432	1,443	1,458
Separations and redundancies	38	39	39	40	40
Workers compensation premiums	1,641	1,708	1,804	1,916	2,034
Other	798	821	833	846	856
Total employee and superannuation liability	**96,295**	**97,346**	**100,614**	**103,818**	**107,262**

Note 14: Grants payable

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
State and Territory governments	3,679	3,929	4,174	4,436	4,704
Non-profit organisations	34	25	20	20	20
Private sector	57	57	47	47	45
Overseas	828	1,333	1,193	965	1,124
Local governments	1	1	1	1	1
Other	4,405	4,471	4,567	4,736	4,874
Total grants payable	**9,004**	**9,816**	**10,003**	**10,204**	**10,768**

Note 15: Net asset movements

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Opening net assets	**-48,075**	**-45,133**	**-45,579**	**-45,075**	**-33,386**
Operating result after extraordinary items	2,707	-355	474	11,594	11,481
Asset revaluation reserve	260	-46	63	105	130
Other movements	-25	-45	-33	-10	-19
Closing net assets	**-45,133**	**-45,579**	**-45,075**	**-33,386**	**-21,794**

Note 16: Taxation receipts — cash AAS31

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Total taxation receipts	203,994	214,352	224,334	236,364	248,995
less payments to States and Territories in relation to GST revenue	33,240	34,460	36,610	38,720	40,850
less payments to States and Territories in relation to mirror tax revenue	312	331	348	365	384
Taxation receipts	**170,442**	**179,561**	**187,376**	**197,279**	**207,761**

APPENDIX A: ADDITIONAL AGENCY STATISTICS

Table A1: General government expenses by agency

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	1,997	2,221	1,612	1,470	1,352
Grains Research and Development Corporation	124	128	132	135	135
Total	**2,121**	**2,349**	**1,743**	**1,605**	**1,488**
Attorney-General's					
Attorney-General's Department	556	477	440	468	486
Australian Customs Service	789	880	889	828	743
Australian Federal Police	680	957	795	792	798
Family Court of Australia	121	122	124	125	126
High Court of Australia	12	12	12	12	12
Total	**2,158**	**2,448**	**2,260**	**2,225**	**2,165**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	602	527	506	394	347
Australian Broadcasting Authority (Administered)	18	17	18	18	17
Australian Broadcasting Corporation	921	992	973	967	981
Australian Communications Authority (Administered)	64	61	61	59	60
Australian Sports Commission	143	146	149	148	151
National Archives of Australia	66	67	67	67	68
National Gallery of Australia	38	40	39	40	41
National Library of Australia	59	60	61	61	61
National Museum of Australia	43	44	43	43	44
Special Broadcasting Service Corporation	185	201	208	206	209
Total	**2,140**	**2,153**	**2,124**	**2,004**	**1,978**
Defence					
Department of Defence	18,311	18,505	18,072	18,628	19,627
Defence Housing Authority	769	761	933	803	812
Total	**19,080**	**19,266**	**19,005**	**19,431**	**20,439**
Education, Science and Training					
Department of Education, Science and Training	14,864	15,689	16,658	17,676	18,456
Australian National Training Authority	1,211	1,213	1,242	1,268	1,319
Australian Research Council	451	538	601	557	625
Australian Nuclear Science and Technology Organisation	160	153	168	167	172
Commonwealth Scientific and Industrial Research Organisation	939	909	959	1,020	1,066
Total	**17,626**	**18,502**	**19,629**	**20,688**	**21,637**
Employment and Workplace Relations					
Department of Employment and Workplace Relations	1,788	1,826	1,830	1,879	1,931
Comcare	278	240	255	273	284
Total	**2,066**	**2,066**	**2,085**	**2,152**	**2,216**

Table A1: General government expenses by agency (continued)

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Environment and Heritage					
Department of Environment and Heritage	524	587	582	570	541
Australian Greenhouse Office	97	117	119	113	105
Bureau of Meteorology	213	205	215	219	223
Total	**834**	**909**	**916**	**902**	**868**
Family and Community Services					
Department of Family and Community Services	67,099	68,847	71,769	74,972	78,301
Centrelink	2,172	2,209	2,190	2,177	2,215
Total	**69,271**	**71,055**	**73,959**	**77,149**	**80,516**
Finance and Administration					
Department of Finance and Administration	4,476	5,124	5,577	6,002	6,068
Australian Electoral Commission	111	219	104	103	222
Total	**4,588**	**5,343**	**5,681**	**6,105**	**6,290**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	891	886	858	860	842
Australian Agency for International Development	1,379	2,166	1,472	1,403	1,824
Australian Trade Commission	345	342	335	335	337
Total	**2,615**	**3,394**	**2,665**	**2,598**	**3,003**
Health and Ageing					
Department of Health and Ageing	34,540	36,248	37,690	39,364	41,412
Health Insurance Commission	560	540	543	556	566
National Blood Authority	464	508	503	503	503
Total	**35,564**	**37,296**	**38,736**	**40,423**	**42,481**
Immigration and Multicultural and Indigenous Affairs					
Department of Immigration and Multicultural and Indigenous Affairs	1,120	2,600	2,654	2,701	2,742
Aboriginal and Torres Strait Islander Commission	233	0	0	0	0
Aboriginal and Torres Strait Islanders Land Fund	0	0	0	0	0
Aboriginal and Torres Strait Islander Services	1,132	0	0	0	0
Total	**2,485**	**2,600**	**2,654**	**2,701**	**2,742**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	1,783	1,928	1,811	1,666	1,652
Australian Tourist Commission	124	145	146	143	144
Total	**1,907**	**2,074**	**1,957**	**1,809**	**1,797**
Parliament					
Joint House Department	46	0	0	0	0
Department of Parliamentary Services	69	147	148	150	153
Total	**115**	**147**	**148**	**150**	**153**
Prime Minister and Cabinet					
Department of the Prime Minister and Cabinet	94	81	73	70	70
Total	**94**	**81**	**73**	**70**	**70**

Table A1: General government expenses by agency (continued)

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Transport and Regional Services					
Department of Transport and Regional Services	4,112	3,980	3,841	4,078	4,133
Civil Aviation Safety Authority	111	115	106	107	107
National Capital Authority	31	28	29	29	29
Total	**4,254**	**4,123**	**3,976**	**4,214**	**4,269**
Treasury					
Department of the Treasury(a)	1,158	1,486	1,155	367	372
Australian Bureau of Statistics	272	287	317	397	303
Australian Securities and Investment Commission	248	246	237	235	246
Australian Taxation Office(a)	8,743	9,033	9,892	9,997	10,211
Australian Office of Financial Management	5,634	5,985	5,916	5,496	5,149
Total	**16,054**	**17,037**	**17,517**	**16,492**	**16,281**
Veterans' Affairs					
Department of Veterans' Affairs	9,979	10,592	11,013	11,392	11,818
Australian War Memorial	-2	39	39	39	40
Total	**9,977**	**10,630**	**11,052**	**11,431**	**11,858**
Small agencies	**2,579**	**2,820**	**2,856**	**2,868**	**2,848**
Whole of government and inter-agency amounts(b)	**-7,839**	**-7,629**	**-5,095**	**-419**	**2,133**
Total expenses	**187,689**	**196,663**	**203,940**	**214,598**	**225,230**

(a) Excludes GST expenses consistent with the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations*, whereby GST is collected by the Australian Taxation Office as an agent for the States and Territories, and appropriated to the States and Territories by the Department of the Treasury.

(b) Estimates of inter-agency transactions are included in the whole of government and inter-agency amounts. The entry for each portfolio does not include eliminations for inter-agency transactions within that portfolio.

Table A2: Departmental expenses by agency

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	489	508	390	375	362
Grains Research and Development Corporation	124	128	132	135	135
Total	**613**	**636**	**521**	**511**	**497**
Attorney-General's					
Attorney-General's Department	184	162	136	131	134
Australian Customs Service	789	880	889	827	743
Australian Federal Police	680	957	795	792	798
Family Court of Australia	121	122	124	125	126
High Court of Australia	12	12	12	12	12
Total	**1,786**	**2,133**	**1,955**	**1,887**	**1,813**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	110	113	114	113	110
Australian Broadcasting Authority (Administered)	18	17	18	18	17
Australian Broadcasting Corporation	844	915	897	890	904
Australian Communications Authority (Administered)	64	61	61	59	60
Australian Sports Commission	143	146	149	148	151
National Archives of Australia	66	67	67	67	68
National Gallery of Australia	38	40	39	40	41
National Library of Australia	59	60	61	61	61
National Museum of Australia	43	44	43	43	44
Special Broadcasting Service Corporation	185	201	208	206	209
Total	**1,571**	**1,662**	**1,655**	**1,646**	**1,664**
Defence					
Department of Defence	16,294	16,168	15,635	16,191	16,990
Defence Housing Authority	769	761	933	803	812
Total	**17,063**	**16,929**	**16,568**	**16,994**	**17,802**
Education, Science and Training					
Department of Education, Science and Training	261	274	276	282	280
Australian National Training Authority	21	15	14	13	13
Australian Research Council	13	13	13	13	13
Australian Nuclear Science and Technology Organisation	160	153	168	167	172
Commonwealth Scientific and Industrial Research Organisation	939	909	959	1,020	1,066
Total	**1,395**	**1,363**	**1,430**	**1,496**	**1,545**
Employment and Workplace Relations					
Department of Employment and Workplace Relations	442	411	444	472	476
Comcare	278	240	255	273	284
Total	**720**	**652**	**699**	**745**	**760**

Table A2: Departmental expenses by agency (continued)

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Environment and Heritage					
Department of Environment and Heritage	253	258	260	264	235
Australian Greenhouse Office	79	45	45	47	47
Bureau of Meteorology	213	205	215	219	223
Total	**545**	**508**	**520**	**530**	**505**
Family and Community Services					
Department of Family and Community Services	2,488	2,633	2,622	2,595	2,642
Centrelink	2,172	2,209	2,190	2,177	2,215
Total	**4,660**	**4,842**	**4,812**	**4,771**	**4,857**
Finance and Administration					
Department of Finance and Administration	381	418	416	565	566
Australian Electoral Commission	111	175	104	103	175
Total	**493**	**592**	**520**	**668**	**741**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	687	659	651	678	661
Australian Agency for International Development	72	73	72	72	73
Australian Trade Commission	195	191	184	185	187
Total	**954**	**923**	**907**	**935**	**920**
Health and Ageing					
Department of Health and Ageing	1,170	678	669	671	679
Health Insurance Commission	560	540	543	556	566
National Blood Authority	7	7	5	5	5
Total	**1,737**	**1,225**	**1,217**	**1,232**	**1,249**
Immigration and Multicultural and Indigenous Affairs					
Department of Immigration and Multicultural and Indigenous Affairs	822	1,182	1,203	1,212	1,231
Aboriginal and Torres Strait Islander Commission	54	0	0	0	0
Aboriginal and Torres Strait Islanders Land Fund	0	0	0	0	0
Aboriginal and Torres Strait Islander Services	161	0	0	0	0
Total	**1,037**	**1,182**	**1,203**	**1,212**	**1,231**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	255	307	300	283	283
Australian Tourist Commission	124	145	146	143	144
Total	**379**	**452**	**446**	**426**	**427**
Parliament					
Joint House Department	24	0	0	0	0
Department of Parliamentary Services	54	110	111	112	115
Total	**78**	**110**	**111**	**112**	**115**
Prime Minister and Cabinet					
Department of the Prime Minister and Cabinet	58	57	57	56	57
Total	**58**	**57**	**57**	**56**	**57**

Table A2: Departmental expenses by agency (continued)

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Transport and Regional Services					
Department of Transport and Regional Services	255	199	185	184	182
Civil Aviation Safety Authority	111	115	106	107	107
National Capital Authority	21	20	20	20	20
Total	**388**	**333**	**311**	**311**	**309**
Treasury					
Department of the Treasury	152	159	156	157	158
Australian Bureau of Statistics	272	287	317	397	303
Australian Securities and Investment Commission	203	207	195	195	197
Australian Taxation Office	2,317	2,419	2,423	2,451	2,472
Australian Office of Financial Management	8	8	8	8	8
Total	**2,951**	**3,080**	**3,100**	**3,208**	**3,139**
Veterans' Affairs					
Department of Veterans' Affairs	312	320	318	328	334
Australian War Memorial	-2	39	39	39	40
Total	**310**	**358**	**357**	**367**	**374**
Small agencies	**2,579**	**2,820**	**2,856**	**2,868**	**2,848**
Whole of government and inter-agency amounts(a)	**23**	**121**	**98**	**95**	**77**
Total departmental expenses	**39,339**	**39,978**	**39,344**	**40,071**	**40,930**

(a) Estimates of inter-agency transactions are included in the whole of government and inter-agency amounts. The entry for each portfolio does not include eliminations for inter-agency transactions within that portfolio.

Table A3: Net capital investment by agency

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	1.7	0.8	-0.2	-8.8	0.0
Grains Research and Development Corporation	0.1	-0.3	-0.2	-0.2	-0.1
Total	**1.8**	**0.5**	**-0.4**	**-9.0**	**-0.1**
Attorney-General's					
Attorney-General's Department	2.0	2.0	10.1	13.7	-3.7
Australian Customs Service	64.8	14.2	-0.6	-0.5	-0.5
Australian Federal Police	6.4	64.4	28.5	-9.4	-11.1
Family Court of Australia	-0.5	0.3	-1.2	-0.1	-0.1
High Court of Australia	0.1	1.4	-0.2	-0.2	-0.2
Total	**72.7**	**80.9**	**36.9**	**3.7**	**-15.5**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	-258.8	-3.2	-2.3	-1.9	-2.2
Australian Broadcasting Authority (Administered)	1.2	-0.7	-0.7	-1.2	-0.5
Australian Broadcasting Corporation	-9.0	-42.9	0.0	0.0	0.0
Australian Communications Authority (Administered)	4.4	-2.7	-2.8	-4.2	-0.9
Australian Sports Commission	-0.7	22.9	16.6	8.2	-6.6
National Archives of Australia	-7.6	-6.4	-5.5	-6.7	-6.3
National Gallery of Australia	7.1	7.5	28.1	5.5	5.3
National Library of Australia	2.9	4.2	7.4	0.7	0.7
National Museum of Australia	-5.9	-3.5	-1.6	-1.6	-1.6
Special Broadcasting Service Corporation	6.0	2.4	2.1	-6.5	-6.6
Total	**-260.3**	**-22.4**	**41.2**	**-7.7**	**-18.6**
Defence					
Department of Defence	-400.1	84.6	959.5	1,187.2	1,404.8
Defence Housing Authority	39.7	39.7	-6.2	88.3	71.8
Total	**-360.4**	**124.4**	**953.3**	**1,275.5**	**1,476.6**
Education, Science and Training					
Department of Education, Science and Training	42.5	3.3	2.1	1.5	0.2
Australian National Training Authority	0.2	0.0	0.0	0.0	0.0
Australian Research Council	0.5	-0.1	-0.3	-0.3	-0.3
Australian Nuclear Science and Technology Organisation	95.0	84.9	79.3	3.7	2.0
Commonwealth Scientific and Industrial Research Organisation	-23.0	18.2	4.5	5.3	39.3
Total	**115.3**	**106.3**	**85.6**	**10.2**	**41.2**
Employment and Workplace Relations					
Department of Employment and Workplace Relations	16.5	-1.7	1.6	1.8	1.9
Comcare	0.0	0.0	0.0	0.0	0.0
Total	**16.5**	**-1.7**	**1.6**	**1.8**	**1.9**

Table A3: Net capital investment by agency (continued)

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Environment and Heritage					
Department of Environment and Heritage	6.2	-4.2	-6.7	-6.7	-23.9
Australian Greenhouse Office	-0.1	-0.1	0.0	0.0	0.0
Bureau of Meteorology	7.2	9.8	8.8	10.8	7.1
Total	**13.3**	**5.5**	**2.1**	**4.1**	**-16.9**
Family and Community Services					
Department of Family and Community Services	-6.7	3.1	-6.9	-4.7	-6.4
Centrelink	1.3	54.8	-15.7	3.5	-15.4
Total	**-5.4**	**57.9**	**-22.6**	**-1.2**	**-21.8**
Finance and Administration					
Department of Finance and Administration	6.2	120.6	-30.2	39.9	-97.7
Australian Electoral Commission	2.6	-0.9	-4.3	-1.5	-0.5
Total	**8.8**	**119.8**	**-34.5**	**38.5**	**-98.2**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	-39.8	-71.4	39.2	30.3	28.7
Australian Agency for International Development	2.0	4.6	-1.2	-0.2	-0.7
Australian Trade Commission	0.0	0.9	-0.6	-0.6	-0.5
Total	**-37.7**	**-65.9**	**37.4**	**29.5**	**27.5**
Health and Ageing					
Department of Health and Ageing	164.8	36.2	5.3	5.8	-4.8
Health Insurance Commission	10.5	9.4	2.8	2.1	1.4
National Blood Authority	21.8	2.1	-0.1	0.0	0.0
Total	**197.1**	**47.7**	**7.9**	**7.8**	**-3.4**
Immigration and Multicultural and Indigenous Affairs					
Department of Immigration and Multicultural and Indigenous Affairs	36.8	141.1	180.9	6.0	53.5
Aboriginal and Torres Strait Islander Commission	-56.7	-45.3	0.0	0.0	0.0
Aboriginal and Torres Strait Islanders Land Fund	0.0	0.0	0.0	0.0	0.0
Aboriginal and Torres Strait Islander Services	57.0	-57.0	0.0	0.0	0.0
Total	**37.0**	**38.8**	**180.9**	**6.0**	**53.5**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	5.5	10.9	-6.3	-10.1	-2.9
Australian Tourist Commission	3.7	0.8	-1.5	0.0	-2.0
Total	**9.2**	**11.7**	**-7.8**	**-10.2**	**-5.0**
Parliament					
Joint House Department	-1,461.9	0.0	0.0	0.0	0.0
Department of Parliamentary Services	1,500.2	-16.1	-28.7	-28.7	-30.8
Total	**38.3**	**-16.1**	**-28.7**	**-28.7**	**-30.8**
Prime Minister and Cabinet					
Department of the Prime Minister and Cabinet	2.9	-0.3	-0.3	-0.2	-0.2
Total	**2.9**	**-0.3**	**-0.3**	**-0.2**	**-0.2**

Table A3: Net capital investment by agency (continued)

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Transport and Regional Services					
Department of Transport and Regional Services	3.7	12.1	5.7	-7.4	-10.7
Civil Aviation Safety Authority	7.9	1.9	3.6	-6.7	-6.8
National Capital Authority	5.8	7.8	1.9	-2.8	-4.4
Total	**17.4**	**21.8**	**11.2**	**-16.8**	**-21.9**
Treasury					
Department of the Treasury	-151.7	-397.1	0.3	1.3	13.2
Australian Bureau of Statistics	-3.2	-3.7	1.1	-5.8	-8.7
Australian Securities and Investment Commission	2.1	0.3	-0.7	1.1	-1.6
Australian Taxation Office	42.4	15.6	20.8	8.3	8.3
Australian Office of Financial Management	-0.7	-0.8	-0.8	-0.8	2.3
Total	**-111.2**	**-385.6**	**20.7**	**4.1**	**13.4**
Veterans' Affairs					
Department of Veterans' Affairs	9.1	4.1	4.5	0.8	-3.7
Australian War Memorial	145.4	3.3	7.6	7.1	-3.2
Total	**154.5**	**7.3**	**12.1**	**7.9**	**-7.0**
Small agencies	**199.2**	**36.9**	**29.8**	**36.0**	**9.3**
Whole of government and inter-agency amounts(a)	**11.3**	**-9.7**	**-298.1**	**-286.8**	**-300.4**
Total net capital investment	**120.3**	**157.9**	**1,028.5**	**1,064.7**	**1,083.7**

(a) Estimates of inter-agency transactions are included in the whole of government and inter-agency amounts. The entry for each portfolio does not include eliminations for inter-agency transactions within that portfolio.

Table A4: Capital appropriations by portfolio

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	32	3	0	0	0
Grains Research and Development Corporation	0	0	0	0	0
Total	**32**	**3**	**0**	**0**	**0**
Attorney-General's					
Attorney-General's Department	5	5	9	11	0
Australian Customs Service	64	19	3	0	0
Australian Federal Police	51	11	19	1	1
Family Court of Australia	0	0	0	0	0
High Court of Australia	0	0	0	0	0
Total	**120**	**35**	**31**	**12**	**1**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	1	0	0	0	0
Australian Broadcasting Authority (Administered)	0	0	0	0	0
Australian Broadcasting Corporation	20	0	0	0	0
Australian Communications Authority (Administered)	0	0	0	0	0
Australian Sports Commission	4	12	18	11	0
National Archives of Australia	2	0	0	0	0
National Gallery of Australia	5	4	25	4	4
National Library of Australia	1	4	7	1	1
National Museum of Australia	0	0	0	0	0
Special Broadcasting Service Corporation	7	6	6	5	4
Total	**41**	**25**	**56**	**21**	**9**
Defence					
Department of Defence	618	299	876	1,104	1,319
Defence Housing Authority	0	0	0	0	0
Total	**618**	**299**	**876**	**1,104**	**1,319**
Education, Science and Training					
Department of Education, Science and Training	5	0	0	0	0
Australian National Training Authority	0	0	0	0	0
Australian Research Council	0	0	0	0	0
Australian Nuclear Science and Technology Organisation	85	43	20	0	0
Commonwealth Scientific and Industrial Research Organisation	0	0	0	0	0
Total	**90**	**43**	**20**	**0**	**0**
Employment and Workplace Relations					
Department of Employment and Workplace Relations	0	0	0	0	0
Comcare	0	0	0	0	0
Total	**0**	**0**	**0**	**0**	**0**

Table A4: Capital appropriations by portfolio (continued)

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Environment and Heritage					
Department of Environment and Heritage	4	0	0	0	0
Australian Greenhouse Office	0	0	0	0	0
Bureau of Meteorology	6	9	9	11	7
Total	**11**	**9**	**9**	**11**	**7**
Family and Community Services					
Department of Family and Community Services	1	1	1	0	0
Centrelink	41	24	34	25	15
Total	**42**	**24**	**34**	**25**	**15**
Finance and Administration					
Department of Finance and Administration	824	1,003	938	864	819
Australian Electoral Commission	2	7	0	0	0
Total	**826**	**1,010**	**938**	**864**	**819**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	27	19	11	9	2
Australian Agency for International Development	209	97	34	22	13
Australian Trade Commission	1	2	0	0	0
Total	**237**	**119**	**46**	**31**	**16**
Health and Ageing					
Department of Health and Ageing	181	60	52	52	48
Health Insurance Commission	34	14	3	2	1
National Blood Authority	0	0	0	0	0
Total	**215**	**75**	**55**	**54**	**49**
Immigration and Multicultural and Indigenous Affairs					
Department of Immigration and Multicultural and Indigenous Affairs	15	69	22	29	25
Aboriginal and Torres Strait Islander Commission	92	0	0	0	0
Aboriginal and Torres Strait Islanders Land Fund	0	0	0	0	0
Aboriginal and Torres Strait Islander Services	14	0	0	0	0
Total	**120**	**69**	**22**	**29**	**25**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	100	96	122	13	12
Australian Tourist Commission	10	0	0	0	0
Total	**110**	**96**	**122**	**13**	**12**
Parliament					
Joint House Department	0	0	0	0	0
Department of Parliamentary Services	0	12	0	0	0
Total	**0**	**12**	**0**	**0**	**0**

Table A4: Capital appropriations by portfolio (continued)

	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m	$m
Prime Minister and Cabinet					
Department of the Prime Minister and Cabinet	0	0	0	0	0
Total	**0**	**0**	**0**	**0**	**0**
Transport and Regional Services					
Department of Transport and Regional Services	66	26	18	10	9
Civil Aviation Safety Authority	0	0	0	0	0
National Capital Authority	1	2	2	2	2
Total	**68**	**28**	**19**	**11**	**10**
Treasury					
Department of the Treasury	782	147	105	78	59
Australian Bureau of Statistics	0	0	0	0	0
Australian Securities and Investment Commission	0	11	0	0	0
Australian Taxation Office	0	10	0	0	0
Australian Office of Financial Management	0	0	0	0	0
Total	**783**	**167**	**105**	**78**	**59**
Veterans' Affairs					
Department of Veterans' Affairs	8	0	0	0	0
Australian War Memorial	0	7	3	0	0
Total	**8**	**7**	**3**	**0**	**0**
Small agencies	**0**	**0**	**0**	**0**	**0**
Whole of government and inter-agency amounts(a)	**0**	**0**	**0**	**0**	**0**
Total capital appropriations	**3,321**	**2,021**	**2,337**	**2,255**	**2,342**

(a) Estimates of inter-agency transactions are included in the whole of government and inter-agency amounts. The entry for each portfolio does not include eliminations for inter-agency transactions within that portfolio.

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector

	Average staffing levels		
	2003-04	2004-05	Change
Agriculture, Fisheries and Forestry			
Department of Agriculture, Fisheries and Forestry	3,756	3,832	76
Australian Fisheries Management Authority	125	124	-1
Australian Wine and Brandy Corporation	54	54	0
Cotton Research and Development Corporation	10	11	1
Fisheries Research and Development Corporation	10	10	0
Forest and Wood Products Research and Development Corporation	7	7	0
Grains Research and Development Corporation	47	47	0
Grape and Wine Research and Development Corporation	9	9	0
Land and Water Resources Research and Development Corporation	36	33	-3
Australian Pesticides and Veterinary Medicines Authority	125	125	0
Rural Industries Research and Development Corporation	17	17	0
Sugar Research and Development Corporation	6	6	0
Wheat Export Authority	13	12	-1
Total	**4,215**	**4,287**	**72**
Attorney-General's			
Attorney-General's Department	759	792	33
Administrative Appeals Tribunal	156	158	2
Australian Crime Commission	475	510	35
Australian Customs Service	4,685	4,772	87
Australian Federal Police	3,965	4,081	116
Australian Institute of Criminology	51	51	0
Australian Law Reform Commission	23	22	-1
Australian Security Intelligence Organisation	760	953	193
Australian Transaction Reports Analysis Centre (Austrac)	89	92	3
Criminology Research Council	1	1	0
Crimtrac Agency	44	44	0
Family Court of Australia	680	680	0
Federal Court of Australia	319	319	0
Federal Magistrates Service	86	114	28
High Court of Australia	86	86	0
Human Rights and Equal Opportunity Commission	95	95	0
Insolvency and Trustee Service Australia	244	247	3
National Native Title Tribunal	273	273	0
Office of Film and Literature Classification	50	51	1
Office of Parliamentary Counsel	45	45	0
Office of the Privacy Commissioner	35	35	0
Office of the Director of Public Prosecutions	457	480	23
Total	**13,378**	**13,901**	**523**

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2003-04	2004-05	Change
Communication, Information Technology and the Arts			
Department of Communications, Information Technology and the Arts	664	686	22
Australia Council	126	126	0
Australian Broadcasting Authority	126	119	-7
Australian Broadcasting Corporation	4,200	4,150	-50
Australian Business Arts Foundation	28	29	1
Australian Communications Authority	416	409	-7
Australian Film Commission	271	271	0
Australian Film, Television and Radio School	145	148	3
Australian National Maritime Museum	99	100	1
Australian Sports Commission	455	455	0
Australian Sports Drug Agency	43	38	-5
Bundanon Trust	11	11	0
Film Australia Limited	3	3	0
National Archives of Australia	419	420	1
National Gallery of Australia	225	220	-5
National Library of Australia	443	441	-2
National Museum of Australia	195	195	0
Net Alert			
Special Broadcasting Service Corporation	798	798	0
Australian Government Information Management Office	114	114	0
Total	**8,781**	**8,733**	**-48**
Defence			
Department of Defence	18,356	17,824	-532
Military Reserves	20,864	20,710	-154
Permanent Military	52,225	52,872	647
Defence Housing Authority	750	750	0
Total	**92,195**	**92,156**	**-39**
Education, Science and Training			
Department of Education, Science and Training	1,688	1,705	17
Australian Institute of Marine Science	158	163	5
Australian National Training Authority	100	97	-3
Australian Nuclear Science and Technology Organisation	835	835	0
Australian Research Council	61	64	3
Commonwealth Scientific and Industrial Research Organisation	6,002	6,016	14
Total	**8,844**	**8,880**	**36**
Employment and Workplace Relations			
Department of Employment and Workplace Relations	2,251	2,246	-5
Australian Industrial Registry	258	276	18
Comcare	325	333	8
National Occupational Health and Safety Commission	79	82	3
Equal Opportunity for Women in the Workplace Agency	21	21	0
Total	**2,934**	**2,958**	**24**

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2003-04	2004-05	Change
Environment and Heritage			
Department of the Environment and Heritage	1,226	1,276	50
Australian Greenhouse Office	174	174	0
Australian Heritage Commission	40	0	-40
Director of National Parks	287	275	-12
Great Barrier Reef Marine Park Authority	170	170	0
National Oceans Office	43	44	1
Bureau of Meteorology	1,441	1,401	-40
Sydney Harbour Federation Trust	42	46	4
Total	**3,423**	**3,386**	**-37**
Family and Community Services			
Department of Family and Community Services	4,400	4,400	0
Australian Institute of Family Studies	41	41	0
Centrelink	24,418	24,437	19
Total	**28,859**	**28,878**	**19**
Finance and Administration			
Department of Finance and Administration	891	1,018	128
Australian Electoral Commission	771	807	36
Commonwealth Grants Commission	48	48	0
Commonwealth Superannuation Administration (ComSuper)	350	350	0
Total	**2,060**	**2,223**	**164**
Foreign Affairs and Trade			
Department of Foreign Affairs and Trade	1,913	1,876	-37
AusAID	488	482	-6
Australia-Japan Foundation	6	6	0
Australian Centre for International Agricultural Research	65	65	0
Australian Trade Commission	1,044	1,052	8
Total	**3,516**	**3,481**	**-35**
Health and Ageing			
Department of Health and Ageing	5,151	5,531	380
Aged Care Standards and Accreditation Agency	203	160	-43
Australian Institute of Health and Welfare	183	183	0
Australian Radiation Protection and Nuclear Safety Agency	126	128	2
Food Standards Australia New Zealand	128	128	0
Health Insurance Commission	4,458	4,500	42
Private Health Insurance Administration Council	13	13	0
Private Health Insurance Ombudsman	8	8	0
Professional Services Review	35	35	0
Total	**10,305**	**10,686**	**381**
Immigration and Multicultural and Indigenous Affairs			
Department of Immigration and Multicultural and Indigenous Affairs	4,844	6,378	1,534
Aboriginal and Torres Strait Islander Commission	110	0	-110
Aboriginal and Torres Strait Islander Services	1,222	0	-1,222
Aboriginal Hostels Ltd	405	405	0
Australian Institute of Aboriginal and Torres Strait Islander Studies	92	80	-12
Indigenous Business Australia	17	18	1

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2003-04	2004-05	Change
Immigration and Multicultural and Indigenous Affairs (cont)			
Indigenous Land Corporation	127	130	3
Refugee Review Tribunal	224	224	0
Torres Strait Regional Authority	48	48	0
Migration Review Tribunal	207	207	0
Total	**7,296**	**7,490**	**194**
Industry Tourism and Resources			
Department of Industry, Tourism and Resources	1,550	1,772	222
Geoscience Australia	590	626	36
Australian Tourist Commission	212	223	11
IP Australia	807	809	2
National Standards Commission	32	0	-32
Total	**3,191**	**3,430**	**239**
Parliament			
Department of the Senate	172	172	0
Department of the House of Representatives	170	166	-4
Department of the Parliamentary Library	97	0	-97
Department of Parliamentary Reporting Staff	187	0	-187
Joint House Department	152	0	-152
Department of Parliamentary Services	376	902	526
Total	**1,154**	**1,240**	**86**
Prime Minister and Cabinet			
Department of the Prime Minister and Cabinet	392	392	0
Australian National Audit Office	290	300	10
Australian Public Service Commission	186	189	3
Office of the Inspector-General of Intelligence and Security	5	5	0
Office of National Assessments	65	68	3
Office of the Commonwealth Ombudsman	82	94	12
Office of the Official Secretary to the Governor-General	79	80	1
Total	**1,099**	**1,128**	**29**
Transport and Regional Services			
Department of Transport and Regional Services	1,104	867	-237
Australian Maritime Safety Authority	237	237	0
Civil Aviation Safety Authority	680	680	0
National Capital Authority	85	86	1
Total	**2,106**	**1,870**	**-236**

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2003-04	2004-05	Change
Treasury			
Department of the Treasury	855	834	-21
Australian Bureau of Statistics	2,746	2,684	-62
Australian Competition and Consumer Commission	447	475	28
Australian Office of Financial Management	38	38	0
Australian Prudential Regulation Authority	528	561	33
Australian Securities and Investment Commission	1,498	1,573	75
Australian Taxation Office	20,682	20,511	-171
Corporations and Markets Advisory Committee	3	3	0
National Competition Council	20	20	0
Productivity Commission	195	172	-23
Total	**27,012**	**26,871**	**-141**
Veterans' Affairs			
Department of Veterans' Affairs	2,478	2,460	-18
Australian War Memorial	288	288	0
Total	**2,766**	**2,748**	**-18**

(a) This table includes estimates of ASL provided by general government sector agencies. ASL figures reflect the average number of employees receiving salary or wages over the financial year, with adjustments for casual and part-time staff, to show the full-time equivalent. This also includes non-uniformed staff and overseas personnel.

Statement 11: Statement of Risks

A range of factors may influence the actual budget outcome in future years. The *Charter of Budget Honesty Act 1998* requires these factors be disclosed in a Statement of Risks in each Budget and Mid-Year Economic and Fiscal Outlook. This statement outlines the fiscal risks and the contingent liabilities which may affect the budget balances.

Statement 11: Statement of Risks

The forward estimates of revenue and expenses in the 2004-05 Budget incorporate assumptions and judgments based on the best information available at the time of publication. A range of factors may influence the actual budget outcome in future years. The disclosure of these factors in this statement increases the transparency of the fiscal projections and ensures they remain 'on-balance' estimates.

Events that could affect fiscal outcomes include:

- changes in economic and other parameters;
- matters not included in the fiscal forecasts because of uncertainty about their timing, magnitude and/or likelihood; and
- the realisation of contingent liabilities.

Risks to the Budget

Economic and other parameters

Major short-term influences on expected revenues and expenses typically are changes in forecasts of economic and non-economic parameters. Over the long-term, differences between the economic parameter forecasts and outcomes have not created any clear bias toward understatement or overstatement of revenue, expenses or the budget balance.

Budget Statement 2 discusses the sensitivity of revenue and expense estimates to major economic parameters.

Fiscal risks

Fiscal risks are general developments or specific events that may affect the fiscal outlook. Some developments or events simply raise the possibility of some fiscal impact. In other cases, some fiscal impact may be reasonably certain, but it will not be included in the forward estimates because the timing or magnitude is not known. Fiscal risks may affect expenses and/or revenue and may be positive or negative on revenue, expenses and/or the budget balance. A general risk to the forward estimates is the possible Senate rejection or amendment of budget measures or other legislation before the Parliament. This general risk is not specifically identified elsewhere in this statement because these measures remain Government policy.

Contingent liabilities

Contingent liabilities are now defined by the accounting standard AASB 1044, which came into effect on 1 July 2002. Broadly, they represent possible costs to the Australian Government arising from past events that the outcome of future events will confirm. Contingent liabilities include loan guarantees, non-loan guarantees, warranties, indemnities, uncalled capital and letters of comfort. These possible costs are in addition to those recognised as liabilities in the consolidated financial statements of the Australian Government general government sector.

The Australian Government's major exposure to contingent liabilities arises from legislation guaranteeing certain liabilities of Australian Government controlled financial institutions (the Reserve Bank of Australia and the Export Finance and Insurance Corporation) and the now fully privatised Commonwealth Bank of Australia.

Strategies to manage these exposures aim to ensure the underlying strength and viability of the entities, so that the guarantees are not triggered. Similar strategies may be adopted in relation to entities not subject to explicit guarantees.

Other arrangements govern the entering into, and monitoring of, contingent liabilities, such as indemnities and uncalled capital. Uncalled capital is primarily associated with international financial institutions, such as the International Bank for Reconstruction and Development, the Asian Development Bank and the European Bank for Reconstruction and Development. Arrangements for capital contributions to these institutions, including contingent liabilities, are approved by Parliament, and the Government provides annual reports on the institutions to Parliament.

Consistent with the Australian Bureau of Statistics Government Finance Statistics standards, transactions concerned with the management of international reserves and the monetary system are classified as financing transactions and do not impact on the budget balances. Accordingly, contingent liabilities (and assets) with the International Monetary Fund are not shown.

Details of fiscal risks and contingent liabilities

Fiscal risks and contingent liabilities with a possible impact on the forward estimates greater than $20 million in any one year, or $40 million over the forward estimates period, are listed below.

Information on fiscal risks takes account of Parliament's decisions and other developments until the close of parliamentary business on 30 April 2004. In general, information on contingent liabilities is based on information provided by Australian Government departments and agencies and is current to 31 March 2004 (or later as indicated). However, in some cases, earlier dates are used and are noted in the relevant section.

Information on contingent liabilities is also provided in the annual financial statements of departments and non-budget entities.

FISCAL RISKS — REVENUE

The Government's revenue and policy measure forecasts, like all forecasts, are subject to a margin of error.

However, over the past 20 years the errors associated with the forecasts of cash receipts have not been significantly different from zero and there has been no bias towards either understatement or overstatement. In fact, over this period, the average error was only 0.5 per cent, with the errors varying around this average by a respectable 2.4 per cent. There is not enough data to accurately assess the forecasting performance for accrual revenue.

An implication of the degree of uncertainty surrounding the revenue forecasts is that, while many of the forecasts are reported to the nearest million dollars for budget accounting purposes, they should not be interpreted as implying an equivalent level of forecast precision.

The various risks influencing the accuracy of the revenue forecasts are outlined.

General risks

The forward estimates of revenue are subject to a number of general pressures that can affect revenue collections. These general pressures include tax avoidance, developments in communications technology and workplace arrangements, court decisions and Australian Taxation Office rulings. These pressures may result in a shift in the composition of revenue collected from the various tax bases and/or a change in the size of the tax base. The revenue forecasts include an appropriate allowance for these factors, given the data available.

Specific risks

Renegotiation of withholding tax rates in certain Australian double tax treaties

Australia's double tax treaties with the Netherlands, France, Switzerland, Italy, Norway, Finland, Austria and the Republic of Korea include 'most favoured nation' clauses on rates of withholding tax. Following the commencement of the Protocol to the Australia-United States double tax treaty, the most favoured nation clause in each of these treaties requires Australia to enter into negotiations with that country with a view to providing similar withholding tax treatment to that which Australia agreed with the United States. The countries have been advised about the obligation to renegotiate and formal negotiations, starting with Norway, commenced in November 2003. Depending on the negotiated outcome, changes to these treaties could have positive as well as negative revenue effects.

FISCAL RISKS — EXPENSES

Agriculture, Fisheries and Forestry

Exceptional circumstances assistance for drought-affected farmers

Exceptional circumstances assistance is available, subject to eligibility criteria, to drought-affected farmers by way of interest rate subsidies and/or income support through the Exceptional Circumstances Relief Payment. A return to severe drought conditions could result in higher than expected expenses for these forms of assistance. It is not possible to quantify the cost arising from such potential developments as this depends on intensity, duration and scale of future drought conditions.

Finance and Administration

Asset sales — Telstra

The forward estimates include the effect of the sale of the Australian Government's shareholding in Telstra, noting that the level of proceeds will depend, inter alia, on the prevailing levels of world equity markets at the time of the sale and that the timing of the sale could be adjusted if market levels are considered unlikely to provide an appropriate return to taxpayers. The sale of the Australian Government's remaining shareholding in Telstra is dependent on the passage of legislation through the Parliament.

Health and Ageing

Medicare Benefits Schedule and Pharmaceutical Benefits Scheme

From time to time items are added to or removed from the Medicare Benefits Schedule and Pharmaceutical Benefits Scheme schedules following independent assessments of cost effectiveness. Major new developments in medicines or medical procedures could result in increases in expenses that exceed the provision in the forward estimates. Similarly, significant shifts in usage patterns, which may occur for particular drugs or groups of drugs from time to time, could result in increases in expenses that exceed the provision in the forward estimates. It is not possible to quantify the fiscal risk arising from such potential developments.

Immunisation funding mechanism

Future vaccine technology will result in new vaccines substituting for those already in use (for example, multivalent vaccines which combine several vaccines into one) and, as a consequence, could result in higher unit costs of vaccine within the routine schedule. Given the nature of current vaccine technology and the possible introduction of new vaccines, specific costs cannot be precisely quantified at this stage.

CONTINGENT LIABILITIES — QUANTIFIABLE

Attorney-General's

Indemnities relating to the Air Security Officer programme

The Australian Government has entered into indemnity agreements with Australian airlines that agree to fly aircraft with Air Security Officers on board. The indemnity agreements limit the Australian Government's exposure up to a maximum of $2 billion per incident. The indemnity applies to the extent that any loss is not covered by existing relevant insurance policies held by the airline and only applies where the airline(s) can prove that an action on the part of an Air Security Officer under or in connection with the Air Security Officer programme caused a loss.

Defence

Other guarantees

Defence carries an extensive range of guarantees and undertakings, normally of a short-term nature, relating to business, training activities and other arrangements involving contracts, agreements and other Defence activities. Indemnities issued cover potential losses or damages for which the Australian Government would be liable.

There are 58 instances of contingencies that are either unquantifiable or uncapped, and 64 instances of quantifiable contingencies to the value of $2,287 million. While these contingencies are considered remote, they have been reported in aggregate for completeness.

Employment and Workplace Relations

Special Employee Entitlements Scheme for Ansett group employees

There is an estimated contingent liability of $80.1 million in relation to the Special Employee Entitlements Scheme for Ansett group employees. This scheme was established by the Australian Government on 9 October 2001 under section 22 of the *Air Passenger Ticket Levy (Collection) Act 2001* to provide a safety net arrangement for staff of the Ansett group of companies whose employment was terminated after 12 September 2001 due to their employer's insolvency.

Finance and Administration

Australian Industry Development Corporation

Under the *Australian Industry Development Corporation Act 1970* certain obligations of the Australian Industry Development Corporation (AIDC) are guaranteed by the Australian Government. As at 30 April 2004, AIDC's contingent liabilities, subject to Australian Government guarantee, were approximately $127 million in respect of guarantees and credit risk facilities.

In addition, AIDC had outstanding Australian Government guaranteed borrowings which totalled approximately $973 million as at the most current valuation of 31 December 2003. These borrowing obligations have been matched by AIDC's holdings of Australian Government guaranteed securities of similar value, largely eliminating the Australian Government's guarantee exposure. These securities were purchased on-market by UBS Warburg and paid to AIDC as consideration for UBS Warburg's purchase of AIDC Limited's (a subsidiary of AIDC) financial assets. UBS Warburg manages this borrowing portfolio on behalf of AIDC. The UBS Warburg arrangement also provides a guarantee to cover any cash flow differences between the interest rate and maturity profiles of the matched borrowings and securities, together with any exchange rate movements in the borrowings. The Australian Government's contingent exposure to these borrowings is therefore negligible and is consequently recorded as zero.

ComLand Limited

Bank borrowings by ComLand Limited are explicitly guaranteed by the Australian Government up to a limit of $60 million, comprising $50 million for principal and $10 million for accrued interest and other costs. When the ComLand sale is completed, this guarantee will be terminated.

Department of Finance and Administration litigation

The Department of Finance and Administration is involved in litigation where a counter-claim for damages has been lodged against the Australian Government. The counter-claim, which will be vigorously defended by the Australian Government, seeks damages of $4.3 billion although the basis for this amount is yet to be fully provided.

Sale of Sydney Airports Corporation Limited

An indemnity has been provided to Southern Cross Airports Corporation as purchaser of the Sydney Airports Corporation Limited (SACL) in the event of a liability arising under Chapter 3 of the *Duties Act 1997* (New South Wales) by reason of the sale of shares in SACL constituting a relevant acquisition in a land-rich private corporation. In the event the liability arises it is estimated to be between $221.2 million and $282.8 million.

Foreign Affairs and Trade

Export Finance and Insurance Corporation

The Australian Government guarantees the due payments by Export Finance and Insurance Corporation (EFIC) of money that is, or may at any time become, payable by EFIC to any body other than the Australian Government. The Australian Government also has in place a $200 million callable capital facility available to EFIC on request to cover liabilities, losses and claims. As at 31 March 2004, the Australian Government's total contingent liability was $3,187 million, comprising EFIC's liabilities to third parties ($2,690 million) and EFIC's contracts of insurance and guarantees ($497 million). The National Interest Account accounted for $1,877 million of these liabilities.

Immigration and Multicultural and Indigenous Affairs

Immigration detention services

The contract with GSL (Australia) Pty Ltd (previously Group 4 Falck Global Solutions Pty Ltd) commenced on 1 September 2003. The Australian Government has agreed to limit GSL's exposure under the liability regime of the contract. While the general contract requires GSL to indemnify the Australian Government for certain claims of losses, the Australian Government has agreed to share the risk. Subject to certain conditions, GSL has been indemnified against claims of losses above a fixed amount to a capped amount. Where claims exceed the cap in any financial year, responsibility for the excess reverts to GSL.

A further limitation of liability has been provided in relation to loss or damage to Australian Government property or equipment as a result of the actions of detainees. Under the contract, GSL's liability for detainee damage is subject to an annual limit, unless claims of losses exceed an agreed cap.

Transport and Regional Services

Maritime industry reform

On 18 August 1998, the Australian Government provided a guarantee to cover borrowings made by the Maritime Industry Finance Company Limited to finance redundancy-related payments in the stevedoring and maritime industries. Outstanding borrowings covered by the guarantee as at 31 January 2004 were $121.9 million.

Treasury

Guarantees under the *Commonwealth Bank Sale Act 1995*

Under the terms of the *Commonwealth Bank Sale Act 1995*, the Australian Government has guaranteed various liabilities of the Commonwealth Bank of Australia (CBA), the Commonwealth Bank Officers' Superannuation Corporation (CBOSC) and the Commonwealth Development Bank. The guarantee for the CBA relates to both on and off-balance sheet liabilities. Of the existing contingent liability, 32 per cent involves off-balance sheet liabilities. As at 31 December 2003, the balance of the guarantee was $9.1 billion, a reduction of $164 million from 30 June 2003.

The guarantee for CBOSC covers the due payments of any amount that is payable to or from the Fund, by CBOSC or by the CBA, in respect of a person who was a member, retired member or beneficiary of the Fund immediately before 19 July 1996. Total accrued benefits at 30 June 2003 have been valued at $3.2 billion. The outstanding value subject to the guarantee is estimated to be $3.2 billion.

As of 1 July 1996, the Commonwealth Development Bank ceased to write new business and no additional liabilities are being incurred. The existing contingent liability will gradually decline with the retirement of existing loans and exposures. The revised estimate for the balance of this guarantee was $18.3 million as at 31 December 2003.

Reserve Bank of Australia guarantee

This contingent liability relates to the Australian Government's guarantee of the liabilities of the Reserve Bank of Australia. It is measured as the Bank's total liabilities excluding capital, reserves and Australian Government deposits. The major component of the Bank's liabilities are notes (that is, currency) on issue. As at 31 March 2004, notes on issue totalled $34.3 billion. In total, the guarantee for the Bank was $43.8 billion as at 31 March 2004.

Terrorism insurance — commercial cover

The Government's Scheme for replacement terrorism insurance commenced on 1 July 2003 and will operate until commercial insurance and reinsurance providers recommence provision of terrorism insurance. The Scheme covers commercial property and infrastructure facilities and associated business interruption and public liability.

The Scheme provides for a pool of funds (initially planned to accumulate to about $300 million) funded by reinsurance premiums paid to the Australian Reinsurance Pool Corporation (ARPC). The pool is supplemented by a bank line of credit of $1 billion, underwritten by the Australian Government, as well as a Commonwealth Government indemnity of $9 billion, giving aggregate cover of up to $10.3 billion when the pool is fully funded.

Under the *Terrorism Insurance Act 2003* the Australian Government guarantees the payment of liabilities incurred by the ARPC. The Treasurer has the ability to declare a reduced payout rate to insureds if, in the absence of such a declaration, the Australian Government's liability would exceed $10 billion. While the guarantee to the ARPC is unlimited, the pro rata reduction will be used to try to limit the Australian Government's exposure to $10 billion.

The ARPC may recoup payouts under the Scheme by increasing premiums for terrorism reinsurance, and pass these funds on to the Australian Government. However such repayments to the Australian Government may take some years.

Uncalled capital subscriptions — international financial institutions

This contingent liability relates to the value of the uncalled portion of the Australian Government's shares as at 31 March 2004 in the International Bank for Reconstruction and Development (US$2.8 billion — estimated value A$3.6 billion), the Asian

Development Bank (US$2.4 billion — estimated value A$3.2 billion), the European Bank for Reconstruction and Development (US$81.7 million plus €77.5 million — estimated value A$232.6 million), and the Multilateral Investment Guarantee Agency (US$26.5 million — estimated value A$34.9 million).

Various

Asbestos related disease claims

The Australian Government is facing a number of claims for asbestos related injuries for military and civilian personnel and for former waterside workers. After obtaining independent actuarial advice, the Government has recognised a liability for asbestos related disease (ARD) claims, which was calculated net of apportionment and cross-claims with other defendants. An additional amount has been recognised to reflect the Government's potential liability for the third party share of ARD claims where the Government is joint and severally liable. This amount is an estimate based on the information currently available on ARD claims, however, the Australian Government liability in relation to other defendants' share of ARD claim costs may be less than or greater than this amount.

CONTINGENT LIABILITIES — UNQUANTIFIABLE

Attorney-General's

Native title costs

The Australian Government has offered to assist the states in meeting compensation costs associated with native title. The amounts that might be paid by the Australian Government will be subject to the terms of financial assistance agreements being negotiated with the states, and liabilities arising from the 1998 amendments to the *Native Title Act 1993*. The Australian Government's liability cannot be quantified due to uncertainty about the number and effect of compensable acts, both in the past and in the future, and the value of native title affected by those acts. Similarly, it is not possible to quantify the liability for compensable acts for which the Australian Government may be directly liable.

The Australian Government has also offered to assist the states with the costs of bodies performing native title functions under state legislation. The extent of this assistance will depend on the existence of such bodies, the timing of their recognition and the extent of their use.

Southern Ocean surveillance

The Australian Government provides funding to the Australian Customs Service and the Department of Agriculture, Fisheries and Forestry to conduct armed patrols of Australia's exclusive economic zone in the Southern Ocean. The inherent risk associated with the type of operations and the conditions to be found working in the

Southern Ocean is expected to be covered by existing insurance policies, except in circumstances where the crew is required use armed force. In these circumstances all risk will become uninsurable and will be borne solely by the Australian Government.

Communications, Information Technology and the Arts

Art Indemnity Australia

Art Indemnity Australia is a programme through which the Australian Government indemnifies cultural objects loaned to exhibitions displayed in Australian museums and galleries. The exact amounts involved will vary with the exchange rate applying at the time any claim for loss or damage to an artwork or heritage object loaned from overseas is paid, and the extent of any loss or damage. Most of the Australian Government risk in indemnifying exhibitions is insured through Comcover. Uninsurable risk continues to be borne solely by the Australian Government.

New South Wales Councils

Waverley City Council and a number of other New South Wales Councils brought action in the Federal Court in July 2003 against the Australian Government and other parties. The Councils are seeking compensation for the acquisition of property and other damages in respect of telecommunications installations on, under and over land to which the Councils have title. The statement of claim does not specify the amount of compensation for damages being sought from the Australian Government and other parties.

Defence

ADI Limited — officers and directors' indemnities

Under the sale agreements for ADI Limited, the Australian Government had indemnified the directors, officers and employees for claims and legal costs associated with assistance related to the sale of the Australian Government's shares in the company. The Australian Government has provided an indemnity to ADI Ltd for uninsured losses relating to specific heads of claims.

Australian Submarine Corporation — Australian Government indemnities provided to Electric Boat Corporation under the Services Agreement

In early October 2002 the Department of Defence entered into a Services Agreement with Electric Boat Corporation (EB) and its subsidiary Electric Boat Australia (EBA) to provide technical and commercial support to the Australian Submarine Corporation (ASC) as it transitioned from being a producer of submarines to an agency for through-life support. EB/EBA staff commenced at ASC on 14 October 2002. The Services Agreement will run for three years with up to four annual extensions.

Under this agreement, EB and EBA were provided with a warranty by the Australian Government and ASC, that they had the right to provide EB/EBA with confidential and other information and the Australian Government provided an indemnity to EB and EBA against claims arising from a breach of that warranty.

The Australian Government also indemnified EB and EBA against claims arising from property loss or personal injury resulting from a defect in the operation or performance of a Collins Class submarine, other than caused by unlawful conduct, gross negligence or wilful misconduct of EB or EBA, against claims exceeding the greater of $2 million or profit earned by EB under the agreement.

HMAS *Melbourne* and HMAS *Voyager* damages claims

Former crew members of HMAS *Melbourne* have instituted legal proceedings against the Australian Government claiming damages for injuries allegedly caused by the HMAS *Voyager*/HMAS *Melbourne* collision on 10 February 1964. One hundred and twenty seven claims remain current. Eighty six of the current claims are statute barred under applicable state laws. In those cases, the plaintiffs will require an extension of time prior to progressing their claims for damages. A number of dependency claims arising from that collision have also been foreshadowed by the dependants of deceased former members of the crew of HMAS *Voyager*. Further claims are likely to be made in connection with the collision.

Litigation cases

The Department of Defence is involved in a wide range of litigation and other claims for compensation and/or damages that may result in litigation where the matters have yet to be finalised by negotiation or, where required, litigation. Various claims, the subject of cases that have yet to be heard, are part heard or are subject to an appeal, await a decision on what (if any) damages and/or costs should be paid to the claimant. The litigated and non-litigated claims include common law liability claims and claims arising from complaints to the Human Rights and Equal Opportunity Commission. The litigation includes asbestos claims and claims from injury resulting from the F-111 Deseal/Reseal programmes. Claims have been received for damage caused by the use of Defence Practice Areas and from the presence of unexploded World War II ordnance. In total there are about 400 claims at present, with a value in excess of $195 million. There is identified potential for additional claims from known incidents of non-military asbestos exposure and the F-111 Deseal/Reseal project of some 130 claims with a value of some $30 million. The current and potential asbestos claims noted above are included in the whole of Government contingent liability detailed under the heading asbestos related disease claims.

Finance and Administration

Australian Industry Development Corporation — board members' and management indemnity

The Australian Government has indemnified the Corporation's board members and management against civil claims relating to employment and conduct as directors and management of subsidiary companies. Liability is subject to the terms of the indemnities.

Australian Submarine Corporation — Australian Government shareholding

The Australian Government has indemnified Barry AC Hilson and BACH Pty Ltd in relation to liabilities arising from assistance provided to the Australian Government during the conduct of a review of the Australian Government's shareholding in Australian Submarine Corporation (ASC). This indemnity is ongoing.

Australian Submarine Corporation — directors' indemnities

The Australian Government has indemnified the members of the board of the ASC for any claims and all legal costs arising from the result of the directors acting in accordance with the board's Tasks and Responsibilities including any current and future ministerial directions.

The Australian Government has specifically indemnified the members of the board of the ASC for any claim associated with the provision of information to the Electric Boat Corporation (EB) of the United States. Certain information has been provided to the EB under a Process Agreement between it, the Australian Government and the ASC. This indemnification has been separately extended to include any claim associated with the provision of information to EB and its subsidiary, Electric Boat Australia under the Services Agreement between ASC, the Department of Defence, EB and Electric Boat Australia.

ComLand Limited — land remediation

The Australian Government has indemnified the ComLand Group in the event that the Group incurs certain land remediation expenses where the need for such remediation was not identified when the land was transferred to ComLand. When the ComLand sale is completed, this indemnity will be terminated and replaced with new indemnities with narrower scope.

ComLand Limited — directors' indemnities

An indemnity has been provided to the directors of ComLand Ltd and to ComLand's General Manager and DBYB Pty Ltd, to indemnify them against liabilities incurred in respect of assistance provided to the Australian Government during the ComLand scoping study and subsequent sale process. This indemnity applies to the period between 1 July 2002 and the completion of the ComLand sale process. The Australian Government may also terminate this indemnity upon reasonable notice in writing to the company.

Employment National Limited — board members' and Chief Executive Officer's indemnity

Indemnities by the Australian Government have been provided to Employment National Limited board members and the Chief Executive Officer to protect against civil claims relating to their employment and conduct as directors. These indemnities are ongoing.

Health Insurance Commission

An indemnity has been provided to Commissioners of Health Insurance Commission (HIC) against claims made in connection with HIC's participation in the IT Outsourcing Initiative. The indemnity applies to actions of HIC during the period of the process to outsource the HIC IT infrastructure up to the time that the HIC entered into a contract.

Indemnities for the Reserve Bank of Australia and private sector banks

Under agencies' contracts for transactional banking services, the Australian Government has indemnified the Reserve Bank of Australia and contracted private sector banks. These banks are indemnified against loss and damage arising from error or fraud by the agency, or transactions made with the authority of the agency.

Sydney Airports Corporation Limited, Bankstown, Camden and Hoxton Park Airports and Essendon Airport Limited — directors' indemnities

The Australian Government has indemnified each member of the board of directors of Sydney Airports Corporation Limited, Bankstown Airport Limited, Camden Airport Limited, Hoxton Park Airport Limited and Essendon Airport Limited against claims and costs incurred arising from the conduct of the directors in relation to the sale, or scoping study for the sale of these airports. Where certain company insurances or indemnities exist for the directors in relation to a claim, the Australian Government indemnity cannot be called upon.

Tuggeranong Office Park Pty Ltd

The Australian Government has provided an indemnity to the Tuggeranong Office Park Pty Ltd (TOP) Trustee to meet any shortfall in the redemption of bonds due on 20 August 2008 which cannot be sourced by TOP or the Construction Development Company from the Sinking Fund. A provision has been raised for this shortfall, based on assumptions current at 31 December 2003. The estimate of this provision is subject to movement in the bond market.

Indemnities relating to other asset sales

Indemnities have been given in respect of a range of other asset sales. Details of these indemnities have been provided in previous Budget and Mid-Year Economic and Fiscal Outlook papers and Finance annual reports. For example, see pages 11-12 to 11-20 in the 2003-04 Budget Paper No. 1, and pages 206-212 of the *2002-03 Finance Annual Report*.

Foreign Affairs and Trade

Export Finance and Insurance Corporation — board members' and senior management indemnities

The Australian Government has provided certain indemnities to Export Finance and Insurance Corporation (EFIC) board members and senior management to protect against civil claims and legal expenses for unsuccessful criminal claims relating to the implementation of EFIC's alliance/divestment of its short-term export credit insurance business.

Health and Ageing

Blood and blood products liability cover

A National Managed Fund (NMF) has been established which pools the liability risks associated with the supply of blood and blood products by the Australian Red Cross Blood Service (ARCBS), between the Australian Government and the states. The NMF is covered by a Memorandum of Understanding (MoU) between the Australian Government, states and the ARCBS. This will be amended to incorporate the operations of the National Blood Authority. It provides for the parties to contribute to the NMF taking into account potential claims payments; the level of funds in the NMF and investment earnings; and a prudential allowance for liabilities incurred but not yet the subject of claims. If there are insufficient funds to cover claim costs, the MoU provides for each party to contribute funds in accordance with allocation provisions prevailing at the time. Under the MoU, the blood and blood products liability cover for the ARCBS remains in force until all parties agree to terminate the arrangements from an agreed date.

Commonwealth Serum Laboratories Limited

Commonwealth Serum Laboratories (CSL) Limited is indemnified against claims made by persons who contract specified infections from specified products and against employees contracting asbestos-related injuries. CSL Limited has unlimited cover for most events that occurred before the sale of CSL Limited on 1 January 1994, but has more limited cover for a specified range of events that might occur during the period of the current Plasma Fractionation Agreement. Where cover has not been arranged, the Australian Government may have a contingent liability. Given the open-ended nature of some of the indemnities, damages and risk cannot be quantified.

Exceptional Claims Scheme

In May 2003 the Prime Minister announced the Medical Indemnity Exceptional Claims Scheme to assume liability for 100 per cent of any damages payable against a doctor that exceeds a specified level of cover provided by that doctor's medical indemnity insurer (MII). These arrangements will apply to payouts related to either a single large claim or to multiple claims that in aggregate exceed the cover provided by the doctor's MII, and will apply to claims notified under contracts-based cover since 1 January 2003.

Indemnity relating to smallpox vaccine

On 12 December 2002, the Australian Government took possession of an initial shipment of 50,000 doses of smallpox vaccine as part of the *Incident response capability*. This vaccine, to be used only in emergency situations, was the only type available for large-scale purchase and was manufactured using older style technology. The Government granted an indemnity to the manufacturer covering possible adverse events that could result from the use of the vaccine.

Immigration and Multicultural and Indigenous Affairs

Separation of Aboriginal children from their families in the Northern Territory

Earlier laws, policies and practices in relation to the Australian Government's administration of the Northern Territory led to the separation of certain Indigenous children from their families. There are currently over 2,000 plaintiffs with claims pending against the Australian Government for (largely unspecified) damages in relation to alleged forcible and wrongful separations (mostly by the children of those allegedly forcibly and wrongfully removed). Two claims have proceeded to trial. Both were unsuccessful.

Industry, Tourism and Resources

Liability for damages caused by space activities

Under the United Nations Convention on International Liability for Damage Caused by Space Objects, the Australian Government is liable to pay compensation for damage caused to nationals of other countries by space objects launched from, or by, Australia. The Australian Government requires the responsible party for a space activity approved under the *Space Activities Act 1998* to insure against liability for damage to third parties for an amount not less than the maximum probable loss, up to a maximum of $750 million. Under the Space Activities Act, the Australian Government also accepts liability for damage suffered by Australian nationals, to a maximum value of $3 billion above the insured level.

Snowy Hydro Limited — directors' indemnities

The Australian Government has, together with the co-shareholder Governments of New South Wales and Victoria, indemnified the members of the board of Snowy Hydro Limited for liabilities arising from entering into agreements to implement corporatisation of the Snowy Mountains Hydro-Electric Scheme, and from liabilities to Snowy Hydro Limited at corporatisation. The indemnity will apply to liabilities arising within five years of corporatisation, and for which a claim is notified to the Governments within eleven years of the corporatisation date of 28 June 2002.

Snowy Hydro Limited — water releases

The Australian, New South Wales and Victorian Governments have indemnified Snowy Hydro Limited for liabilities arising from water releases in the Snowy River below Jindabyne Dam, where these releases are in accordance with the water licence and related regulatory arrangements agreed between the three Governments. The indemnity will apply to liabilities for which a claim is notified within 20 years from 28 June 2002.

The Australian, New South Wales and Victorian Governments will provide financial support to the company, if this is necessary, to avoid the company breaching its loan covenants to fund the cost of civil works required to address a cold water pollution offence. The undertaking applies for seven years from 28 June 2002.

Transport and Regional Services

Deep vein thrombosis class action

The Civil Aviation Safety Authority (CASA) has been named in a number of writs, which allege that CASA was negligent in not making air travellers aware of the risks of deep vein thrombosis during long periods of immobility. As at 29 February 2004, there have been 483 writs issued against CASA. The writs span 1995 to 2002. The Australian Government's exposure is limited to claims for the years 1995 to 30 June 1998, as CASA was covered by a Commonwealth Deed of Indemnity in relation to the performance of its regulatory functions. As at 29 February 2004, 108 writs had been issued against CASA which are covered by the Deed of Indemnity. The remaining writs are covered by CASA's commercial insurance.

Maritime Industry Finance Company Limited board members' indemnity

Indemnities for Maritime Industry Finance Company Limited (MIFCo) board members have been provided to protect against civil claims relating to employment and conduct as directors of MIFCo.

Tripartite deeds relating to the sale of core regulated airports

Tripartite deeds apply to the 12 core regulated airports (Sydney, Melbourne, Brisbane, Perth, Canberra, Coolangatta, Townsville, Adelaide, Hobart, Launceston, Darwin and Alice Springs). The tripartite deeds between the Australian Government, the airport lessee company and financiers provide for limited step-in rights for the financiers in circumstances when the airport lease is terminated to enable the financiers to correct the circumstances that triggered such a termination event.

Treasury

Housing Loans Insurance Corporation guarantee

The Australian Government sold the Housing Loans Insurance Corporation (HLIC) on 12 December 1997 and has assumed all residual contingencies. The principal amount covered by the guarantee and the balances outstanding are unable to be reliably measured. The guarantee relates essentially to the HLIC's contracts of mortgage insurance and any borrowings approved by the Treasurer up to the time of sale.

PART 5
PUBLIC SECTOR TRENDS

This part addresses trends in the fiscal balance, cash surplus, and balance sheet data (net debt, net worth and net interest payments) for the Australian and State/local levels of government along with the consolidated non-financial public sector.

STATEMENT 12: TRENDS IN PUBLIC SECTOR FINANCES

This Statement discusses trends in the fiscal balance, cash surplus and balance sheet data (net debt, net worth and net interest payments) for the total non-financial public sector at the Australian and state/local levels of government and also at the consolidated level. These measures are discussed in greater detail in *Statement 8, Financial Reporting Standards and Budget Concepts*.

This Statement provides a broader context in which to consider developments in the Australian Government's Budget.

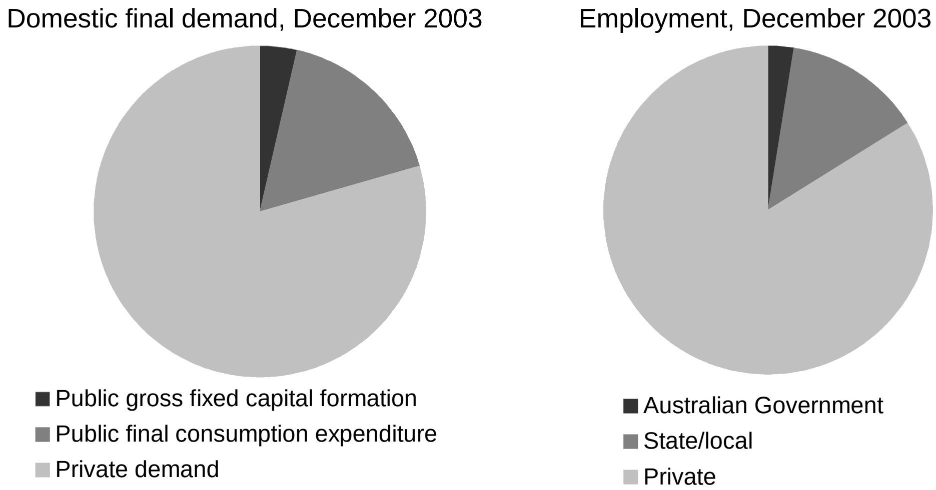
For further information on the data used in the charts and tables in this section see *Appendix B: Data*. This Statement uses the convention that references to the states include the territories and that the combined state and local government sector is denoted as the state/local sector and includes territory governments, unless otherwise stated.

STATEMENT 12: TRENDS IN PUBLIC SECTOR FINANCES

SIZE AND STRUCTURE OF THE PUBLIC SECTOR

The total public sector[1] constitutes a significant portion of the Australian economy (over 20 per cent of domestic final demand). The size and structure of Australia's public sector provides a useful and important context for interpreting the trends in this sector.

Chart 1: Contribution of public and private sectors



Source: ABS Cat. No. 6248.0, 6202.0 and 5206.0.

Domestic final demand (as shown in Chart 1), is made up of public final demand (which comprises public gross fixed capital formation and public final consumption expenditure) and private demand (which comprises private gross fixed capital formation and private final consumption expenditure). The Australian Government constitutes 37 per cent of public final demand, while the state/local level accounts for 63 per cent.

There are significant differences in the roles and responsibilities of the two main levels of government. Major components of the Australian Government's expenses include transfer payments in relation to social security and welfare and defence expenditure.

---

1 The total public sector includes the general government sector, public non-financial corporations sector and the public financial corporations sector for the Australian Government and state/local levels of government.

Transfer payments, such as Australian Government income support payments, are not included in public final demand. Rather, these and other payments that the Australian Government makes to the states and the private sector to assist in funding important services, like education and health, are reflected in either state/local public final demand or private demand.

In terms of employment, the total public sector employs approximately 16 per cent of wage and salary earners (Chart 1). The state/local sector accounts for approximately 13 per cent of all wage and salary earners and for approximately 84 per cent of total public sector wage and salary earners. The Australian Government accounts for approximately 3 per cent of all wage and salary earners and for approximately 16 per cent of total public sector wage and salary earners. This reflects the state/local sector's major responsibilities for service delivery in the areas of education, health, transport and public order and safety.

FISCAL BALANCE

As outlined in Figure 1 of Statement 8, the total public sector is made up of the non-financial public sector (NFPS) and the public financial corporations sector. The NFPS is comprised of the general government sector and the public non-financial corporations (PNFC) sector.

The general government sector forms the majority of the NFPS (particularly in terms of revenues and expenses). The PNFC sector tends to be more important at the state/local level, where most PNFCs are concentrated.

The fiscal balance of the Australian Government general government sector is expected to fall from a surplus of 0.4 per cent of Gross Domestic Product (GDP) in 2003-04 to a surplus of 0.1 per cent of GDP in 2004-05. It is projected that in 2005-06, the fiscal balance of the Australian Government general government sector will maintain a surplus of 0.1 per cent of GDP, rising to a surplus of 0.3 per cent of GDP by 2007-08.

The fiscal balance of the state/local general government sector is expected to be in surplus by 0.1 per cent of GDP in 2003-04, but is projected to move to a small deficit of 0.1 per cent of GDP in 2004-05. This projection is predominantly based on state 2003-04 mid-year reviews since only Victoria, Western Australia and the Australian Capital Territory have released their 2004-05 Budgets.

The consolidated[2] PNFC fiscal balance is expected to be in deficit in 2003-04 (0.2 per cent of GDP). This includes an estimated Australian Government PNFC fiscal balance surplus of 0.2 per cent of GDP. The decrease in consolidated PNFC revenue

2 When combined, the Australian Government and state/local governments and universities are referred to as the 'consolidated public sector'.

and expenses as a share of GDP in recent years is partly attributable to the privatisation of PNFCs by both the Australian and state/local governments.

Tables 1, 2 and 3 show general government, PNFC and NFPS fiscal balance data by level of government respectively.

Table 1: General government fiscal balance by level of government (per cent of GDP)[(a)(b)]

	Australian Government			State/local			Consolidated		
	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance
1996-97	26.7	27.5	-0.8	na	na	na	na	na	na
1997-98	26.2	26.5	-0.4	na	na	na	na	na	na
1998-99	25.7	24.8	0.6	17.5	16.7	0.3	38.0	36.2	1.0
1999-00	26.6	24.7	2.1	17.3	16.4	0.3	38.8	35.9	2.5
2000-01	24.1	23.4	0.9	17.1	16.7	-0.1	38.3	37.1	0.8
2001-02	22.7	23.3	-0.5	16.9	16.5	0.0	36.7	36.7	-0.5
2002-03	23.2	22.4	0.8	17.2	16.5	0.4	38.0	36.5	1.2
2003-04(e)	23.0	22.6	0.4	16.8	16.3	0.1	37.2	36.2	0.6
2004-05(e)	**22.5**	**22.4**	**0.1**	**16.3**	**15.9**	**-0.1**	**36.2**	**35.5**	**0.1**
2005-06(p)	22.2	22.1	0.1	na	na	na	na	na	na
2006-07(p)	22.2	22.0	0.2	na	na	na	na	na	na
2007-08(p)	22.1	21.9	0.3	na	na	na	na	na	na

(a) The fiscal balance is equal to revenue less expenses less net capital investment. Net capital investment is not shown in this table.
(b) Accrual time series data are being reviewed by the ABS, in consultation with all Treasuries in 2004, as accrual reporting is now established in all jurisdictions. This should result in improved quality in time series data, and may result in some changes to these series.
(e) Estimates.
(p) Projections.
na Data not available.

Table 2: Public non-financial corporations' fiscal balance by level of government (per cent of GDP)[(a)(b)]

	Australian Government			State/local			Consolidated		
	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance
1996-97	5.2	4.9	-0.1	na	na	na	na	na	na
1997-98	5.3	4.8	0.4	na	na	na	na	na	na
1998-99	4.7	4.4	-0.1	6.2	6.2	-0.4	10.9	10.6	-0.5
1999-00	4.0	3.7	0.2	5.8	5.5	0.4	9.9	9.2	0.5
2000-01	3.8	3.7	-0.1	5.4	5.2	0.2	9.2	8.8	0.1
2001-02	3.7	3.5	0.1	4.8	4.7	-0.2	8.6	8.3	-0.1
2002-03	3.2	3.0	0.3	4.6	4.6	-0.4	7.9	7.7	-0.1
2003-04(e)	3.1	2.9	0.2	4.4	4.3	-0.4	7.5	7.3	-0.2
2004-05(e)	**3.0**	**2.7**	**0.3**	**na**	**na**	**na**	**na**	**na**	**na**

(a) The fiscal balance is equal to revenue less expenses less net capital investment. Net capital investment is not shown in this table.
(b) Accrual time series data are being reviewed by the ABS, in consultation with all Treasuries in 2004, as accrual reporting is now established in all jurisdictions. This should result in improved quality in time series data, and may result in some changes to these series.
(e) Estimates.
na Data not available.

Table 3: Total Non-financial public sector fiscal balance by level of government (per cent of GDP)[(a)(b)]

	Australian Government			State/local			Consolidated		
	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance
1996-97	na	na	-0.9	na	na	na	na	na	na
1997-98	na	na	0.1	na	na	na	na	na	na
1998-99	29.7	28.5	0.5	21.3	20.5	-0.1	45.8	43.8	0.5
1999-00	30.1	27.7	2.3	21.1	19.9	0.7	46.1	42.4	3.0
2000-01	27.3	26.4	0.8	20.7	20.0	0.0	45.0	43.5	0.8
2001-02	25.8	26.2	-0.4	20.0	19.3	-0.2	42.8	42.5	-0.5
2002-03	25.8	24.8	1.0	20.1	19.3	0.0	43.5	41.6	1.2
2003-04(e)	25.5	24.9	0.6	19.4	18.9	-0.4	42.4	41.1	0.4
2004-05(e)	**25.0**	**24.6**	**0.4**	**na**	**na**	**na**	**na**	**na**	**na**

(a) The fiscal balance is equal to revenue less expenses less net capital investment. Net capital investment is not shown in this table.
(b) Accrual time series data are being reviewed by the ABS, in consultation with all Treasuries in 2004, as accrual reporting is now established in all jurisdictions. This should result in improved quality in time series data, and may result in some changes to these series.
(e) Estimates.
na Data not available.

CASH SURPLUS

General government sector

The Australian Government general government sector has been in surplus since 1997-98, with the exception of a small cash deficit of 0.1 per cent of GDP in 2001-02.

Panels A and C of Chart 2 show the large contribution of past Australian Government general government cash deficits to the consolidated NFPS cash deficit. Panel A also illustrates the improvement in the Australian Government general government sector balance, culminating in the strong surplus outcomes of recent years.

Panel A of Chart 2 shows the sustained improvement in state/local general government balances over the period 1991-92 to 1996-97, from a deficit of 1 per cent of GDP to a cash surplus of 0.6 per cent of GDP. Since then, the state/local sector has maintained surpluses (with the exception of 1998-99). It is estimated that the state/local general government cash surplus will reduce to 0.2 per cent of GDP in 2003-04, compared to 0.6 per cent of GDP in 2002-03. This partly reflects the state governments' expectations of a more subdued property market and hence, reduced state government receipts from property taxes such as conveyancing duty.[3]

Public non-financial corporations sector

The contribution made by the PNFC sector to the cash surplus of the consolidated NFPS has declined from the late 1980s, with the privatisation of government businesses.

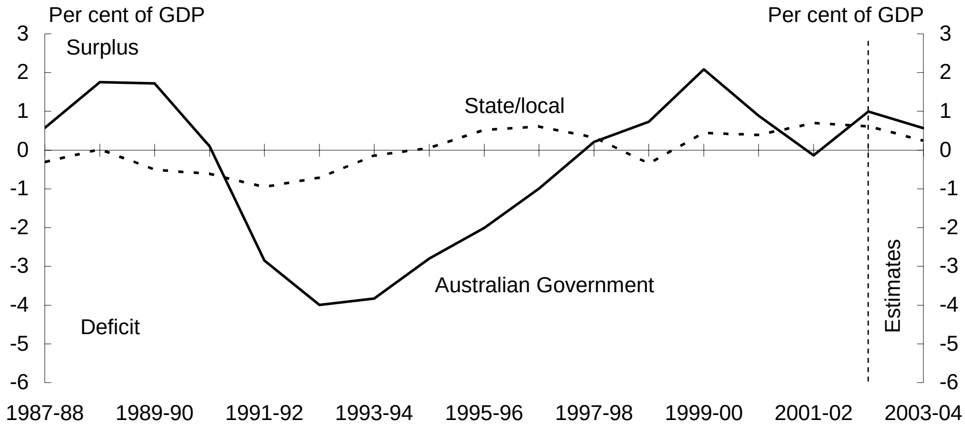
As shown in Chart 3, the consolidated PNFC sector has maintained a cash surplus position through much of the 1990s. The sector is projected to be in deficit in 2003-04, partly due to relatively large deficits in the New South Wales, Victoria, Queensland and Western Australian PNFC sectors.

---

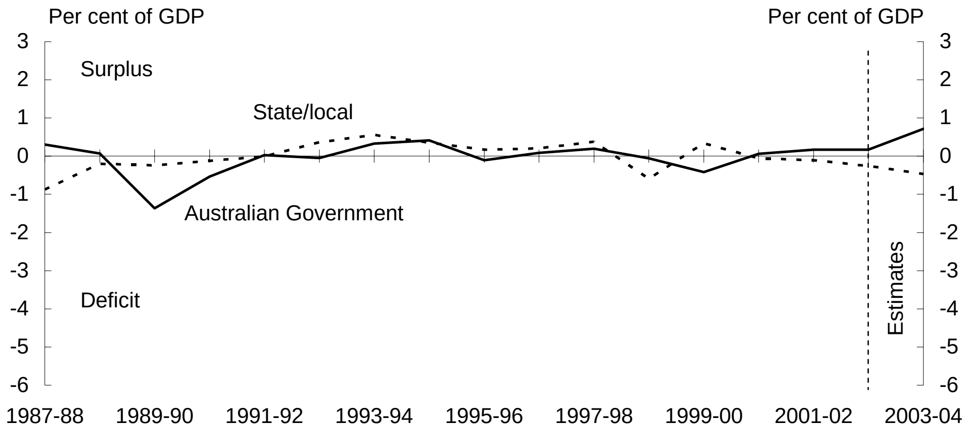
3 As noted in the 2003-04 NSW *Half-Yearly Review*, pages 1, 6-7 and the Victorian 2004-05 Budget Paper No. 2, *Strategy and Outlook*, page 42.

Chart 2: Cash surplus by sector and level of government

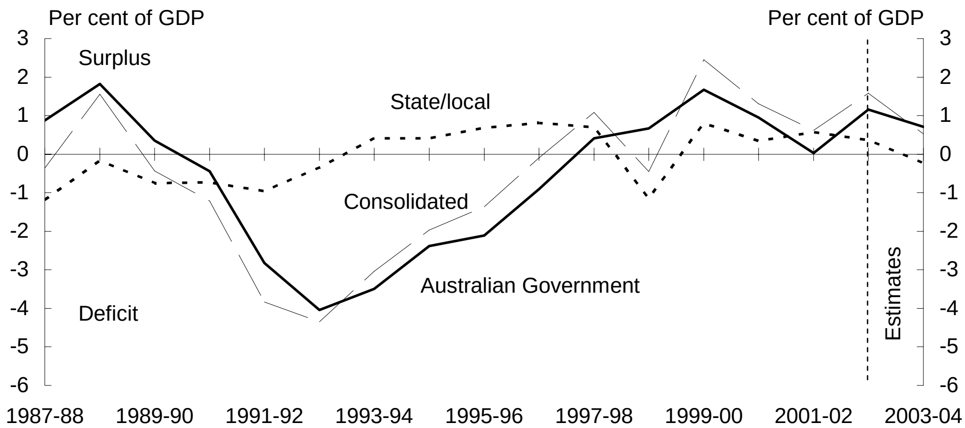
A: General government



B: Public non-financial corporations



C: Non-financial public sector

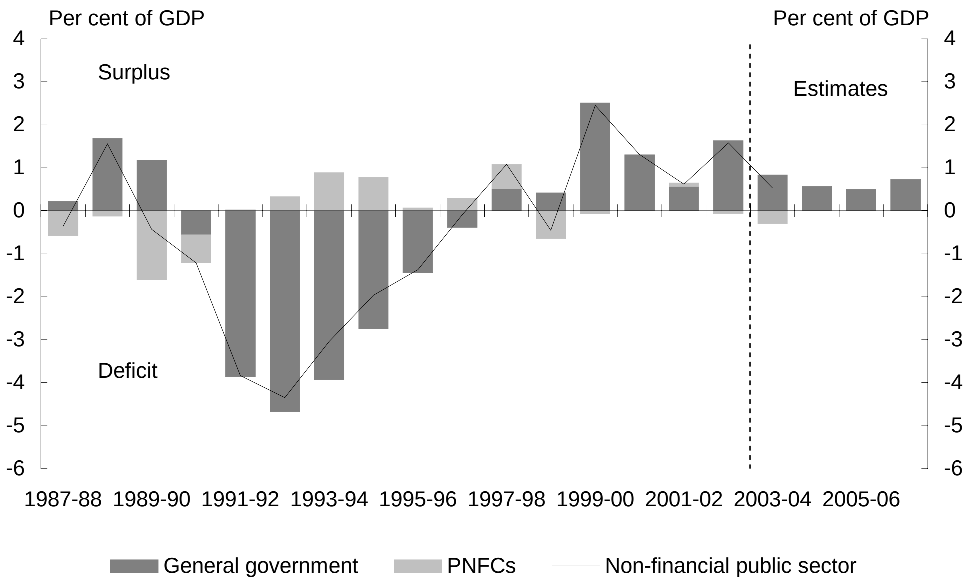


Non-financial public sector

It is estimated that the consolidated NFPS will achieve a cash surplus of 0.5 per cent of GDP in 2003-04.

Chart 3 illustrates that the consolidated NFPS was generally in a deficit position during the early to mid 1990s. The deficit peaked at 4.3 per cent of GDP in 1992-93 before moving into a surplus position in 1997-98. This primarily reflects Australian Government general government cash deficits in the early to mid 1990s. Since 1999-2000, the consolidated NFPS has remained in surplus, due to consecutive surpluses in the consolidated general government sector. The deficit in 1998-99 is the result of one-off increases in state funding of superannuation liabilities.

Chart 3: Consolidated non-financial public sector cash surplus by sector[(a)]



(a) Data for the consolidated PNFCs and NFPS are only available to 2003-04, while general government data is available to 2006-07.

Receipts and payments

Chart 4 shows trends in general government cash receipts and payments at the Australian, state/local and consolidated levels. Due to its size, the general government sector is an appropriate focus for an assessment of public sector receipts and payments. It is also the sector through which governments primarily affect the level of private sector activity.

Australian Government receipts and payments estimates in Panel A of Chart 4 are net of GST receipts and show a decline in 2000-01 with the introduction of *The New Tax System*. In addition, the reform of Australian Government and state/local government taxes resulted in total consolidated general government receipts falling from 38.8 per cent of GDP in 1999-2000 to 37.3 per cent of GDP in 2003-04, partly reflecting significant personal income tax cuts and the abolition of Financial Institutions Duty and stamp duty on quoted marketable securities.

The improvement in state finances from 1991-92 is shown in Panel B of Chart 4. The state/local cash deficit peaked at 1 per cent of GDP in 1991-92. After 1991-92, deficits continued to reduce until the state/local sector achieved a surplus in 1994-95. Since 1994-95, the state/local cash position has been in surplus each year, with the exception of 1998-99. This improvement was initially due to payments restraint, helped by lower debt servicing charges and more recently by the strong growth in revenues related to the property market.

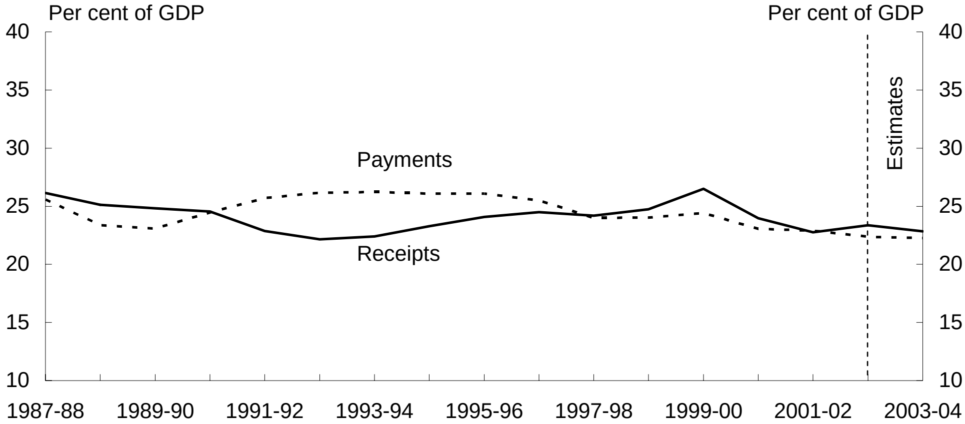
The increases in both receipts and payments in 1998-99 for the state/local sector and in 1999-2000 for the Australian Government sector, shown in Panels A and B of Chart 4, were predominantly due to the move to an accrual accounting framework and the subsequent 'grossing' up of cash receipts and payments, whereas prior to this, some cash receipts were netted off payments.

The PNFC sector is an important provider of economic infrastructure and contributes significant revenue to the general government sector, mainly in the form of dividends. State/local governments account for the majority of total PNFC sector payments, reflecting State responsibility for infrastructure and service provision in areas such as electricity, gas, water and public transport.

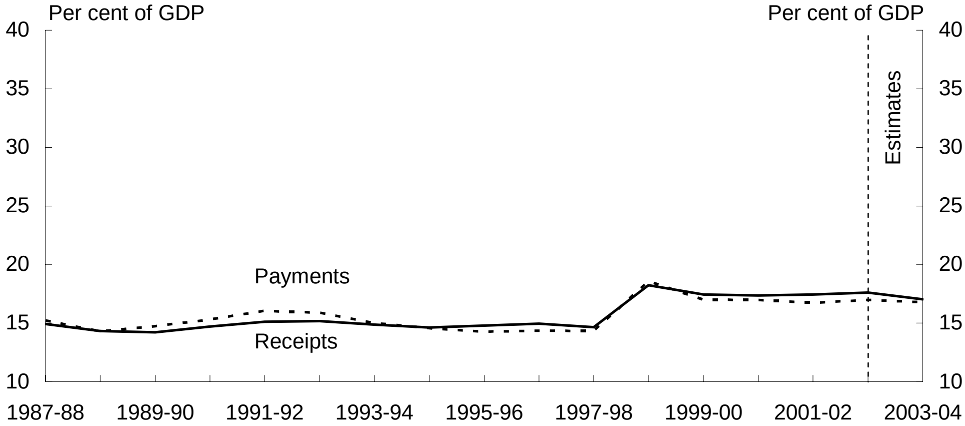
PNFC privatisations over the last decade have occurred in two main sectors — electricity and gas (such as Victorian and South Australian electricity assets) and transport and communications (such as the partial sale of Telstra). Proceeds of asset sales have largely been used to reduce, or contain, the growth of general government net debt, resulting in ongoing savings in public debt interest.

Chart 4: General government receipts and payments by level of government

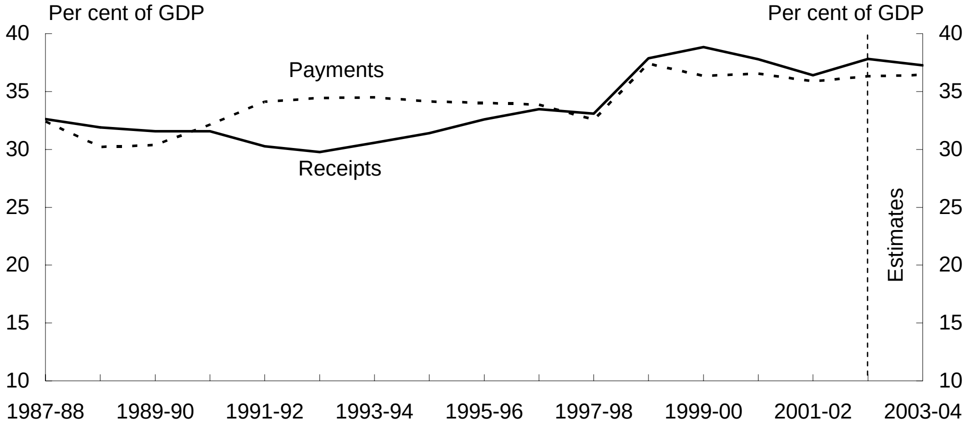
A: Australian Government



B: State/local



C: Consolidated



NET DEBT

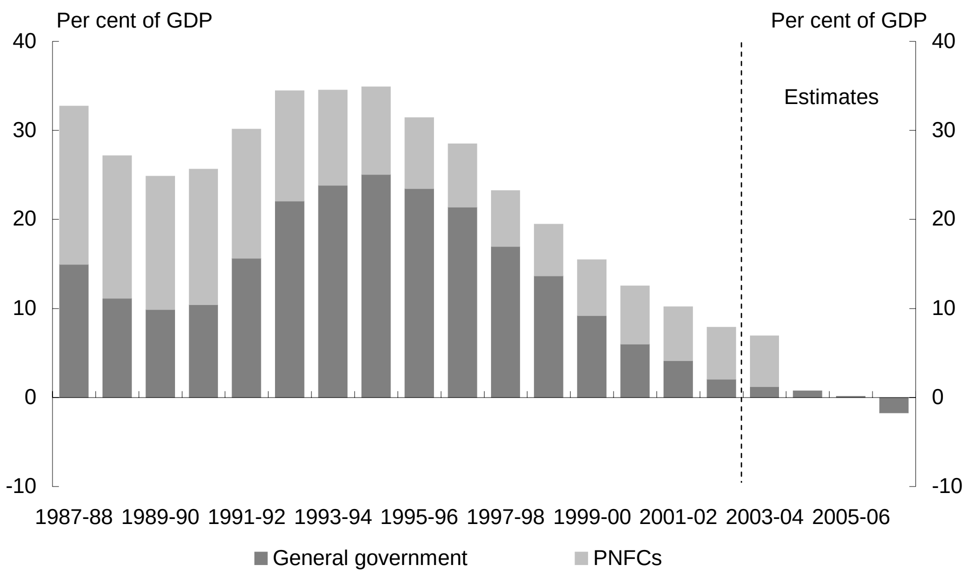
Chart 5 shows that consolidated general government net debt as a share of GDP is expected to continue to decline over the forward estimates period. Consolidated NFPS net debt is estimated to be 6.9 per cent of GDP in 2003-04, compared with the most recent peak of 34.9 per cent in 1994-95.

Charts 3 and 5 show the broad correlation between cash deficits and net debt levels. The financing of Australian Government cash deficits resulted in a substantial increase in general government net debt as a share of GDP over the early 1990s.

Chart 5 also shows the decline in PNFC sector net debt as a share of GDP since the late 1980s, reflecting lower levels of capital expenditure, improved efficiency and privatisations. This decline moderated the increase in NFPS net debt as a share of GDP in the first half of the 1990s.

The subsequent improvement in NFPS net debt primarily reflects both the Australian Government and the state/local sector moving back into budget surpluses and the application of privatisation proceeds to debt retirement at both the Australian Government and state/local government levels.

Chart 5: Consolidated non-financial public sector net debt by sector (as at end of financial year)[(a)]



(a) Data for the consolidated PNFC and NFPS are only available to 2003-04, while general government data is available to 2006-07.

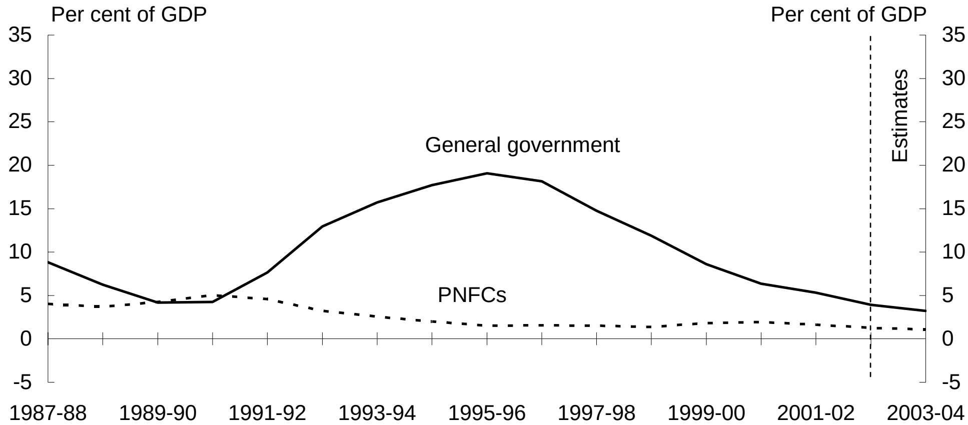
Chart 6 shows that most Australian Government net debt is held by the general government sector whereas almost all state/local net debt is held in the PNFC sector.

As shown in Panel A of Chart 6, Australian Government general government net debt as a share of GDP grew from low levels in the late 1980s to a peak of 19.1 per cent in 1995-96. Successive surpluses and asset sales (most notably the partial sale of Telstra) since then, have reduced Australian Government general government sector net debt to an expected 3.2 per cent of GDP in 2003-04.

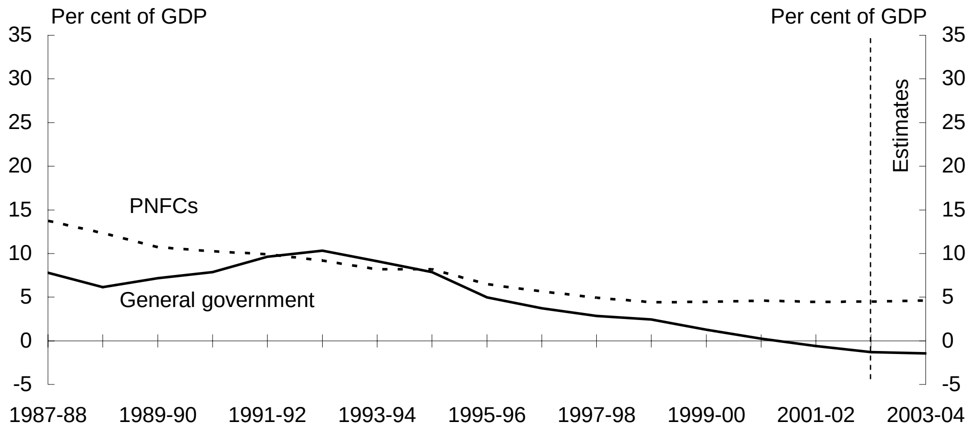
In contrast, state/local general government net debt grew more modestly in the early 1990s and is expected to decline from a peak of 10.3 per cent of GDP in 1992-93 to approximately -1.4 per cent of GDP in 2003-04, as shown in Panel B. This improvement within the state/local general government sector reflects both the impact of asset sales and fiscal consolidation during the second half of the 1990s. However, some individual States continue to face relatively high net debt burdens in either their general government sector or in their PNFC sector (for further information, see Budget Paper No. 3 — *Federal Financial Relations 2004-05*).

Chart 6: Non-financial public sector net debt by level of government and sector (as at end of financial year)

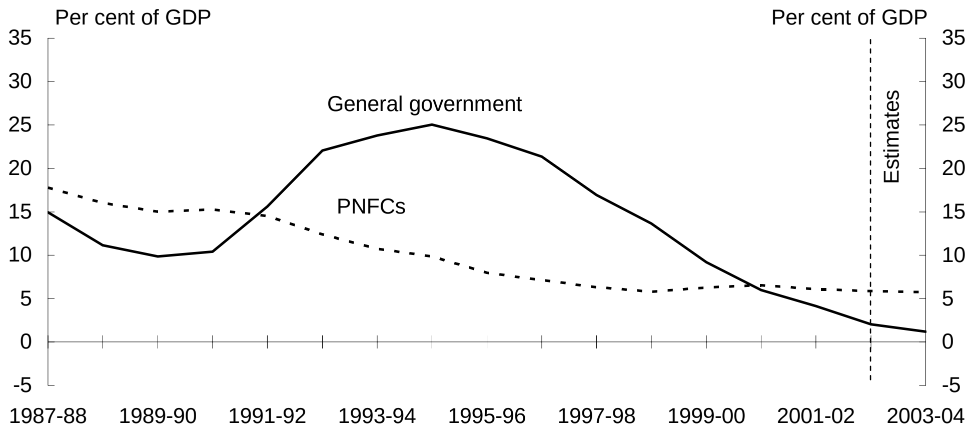
A: Australian Government



B: State/local



C: Consolidated



NET WORTH

The state/local general government sector has an estimated positive net worth of 58.9 per cent of GDP in 2004-05. State/local net worth has increased in nominal terms each year. However, since 1999-2000, net worth has not always grown at the same pace as the economy and hence, represents a decreasing proportion of GDP. The Australian Government general government sector has historically recorded negative net worth. This difference primarily reflects the significant funding provided by the Australian Government to the states and to local government for capital works, with the resultant assets recorded in the states and local governments' balance sheets.

Table 4: General government net worth by level of government (as at end of financial year)[(a)]

	Australian Government(b)		State/local		Consolidated	
	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP
1996-97	-74,354	-14.0	na	na	na	na
1997-98	-68,544	-12.2	na	na	na	na
1998-99	-76,150	-12.9	364,053	61.5	305,967	51.7
1999-00	-39,105	-6.2	391,204	62.5	371,165	59.3
2000-01	-41,769	-6.2	406,127	60.5	384,319	57.3
2001-02	-47,553	-6.7	427,062	59.8	401,386	56.2
2002-03	-51,333	-6.8	468,534	62.1	440,682	58.4
2003-04(e)	-43,545	-5.4	488,054	60.2	470,313	58.0
2004-05(e)	**-42,836**	**-5.0**	**506,318**	**58.9**	**491,133**	**57.2**
2005-06(p)	-42,926	-4.7	na	na	na	na
2006-07(p)	-38,515	-4.0	na	na	na	na
2007-08(p)	-37,434	-3.7	na	na	na	na

(a) Accrual time series data are being reviewed by the ABS, in consultation with all Treasuries in 2004, as accrual reporting is now established in all jurisdictions. This should result in improved quality in time series data, and may result in some changes to these series.

(b) There is a break in the Australian Government net worth series between 1998-99 and 1999-2000. Data up to 1998-99 are sourced from the Commonwealth's Consolidated Financial Statements based on Australian accounting standards. Data beginning in 1999-2000 are based on the GFS framework. For the general government sector, the major change across the break in the series is an improvement in net worth. This is primarily due to the move from valuing investments in public corporations at historic cost to current market value (which is calculated using the share price for listed corporations). This is partly offset by defence weapons platforms no longer being recorded as assets.

(e) Estimates.

(p) Projections.

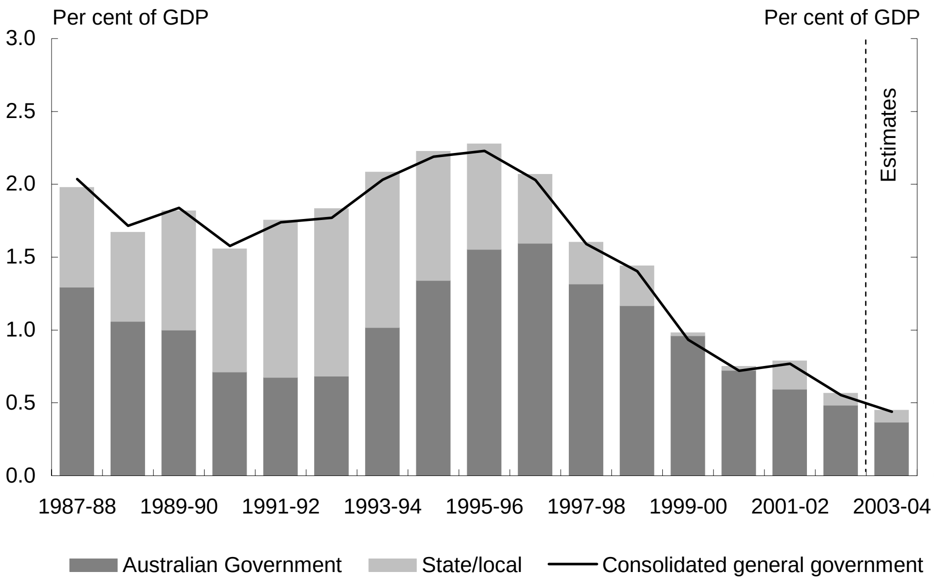
na Data not available.

NET INTEREST PAYMENTS

Consolidated general government net interest payments peaked in 1995-96 at 2.2 per cent of GDP due to the increased level of Australian Government general government net debt. Consolidated net interest payments are expected to fall to 0.4 per cent of GDP in 2003-04 due to reduced Australian and state/local general government net debt since 1995-96 and lower interest rates in recent years.

The contribution of the PNFC sector to NFPS net interest payments has decreased significantly in recent years as reduced investment by PNFCs, improved performance by PNFCs, and privatisations, have reduced PNFC net debt as a share of GDP.

Chart 7: General government net interest payments



APPENDIX A: SUPPLEMENTARY CASH TABLES

Table A1: Consolidated cash receipts, payments and cash surplus by institutional sector as a per cent of GDP[(a)]

	General government			Public non-financial corporations			Non-financial public sector		
	Receipts	Payments	Cash surplus	Receipts	Payments	Cash surplus	Receipts	Payments	Cash surplus
1987-88	32.6	32.4	0.2	4.0	5.9	-0.6	35.5	37.2	-0.4
1988-89	31.9	30.2	1.7	3.8	5.4	-0.1	34.8	34.6	1.6
1989-90	31.6	30.4	1.2	3.7	6.7	-1.6	34.1	36.0	-0.4
1990-91	31.6	32.1	-0.6	3.8	5.9	-0.7	34.2	36.8	-1.2
1991-92	30.3	34.1	-3.9	3.6	5.4	0.0	32.5	38.2	-3.8
1992-93	29.8	34.4	-4.7	3.6	5.0	0.3	32.0	38.1	-4.3
1993-94	30.6	34.5	-3.9	3.8	4.3	0.9	32.7	37.3	-3.0
1994-95	31.4	34.1	-2.7	3.4	4.5	0.8	33.3	37.2	-2.0
1995-96	32.6	34.0	-1.4	3.0	4.5	0.1	33.9	36.9	-1.4
1996-97	33.5	33.9	-0.4	3.1	4.2	0.3	34.4	35.9	-0.1
1997-98	33.1	32.6	0.5	3.0	3.7	0.6	34.4	34.7	1.1
1998-99	37.9	37.4	0.4	na	na	-0.6	na	na	-0.5
1999-00	38.8	36.3	2.5	na	na	-0.1	na	na	2.4
2000-01	37.8	36.5	1.3	na	na	0.0	na	na	1.3
2001-02	36.4	35.9	0.6	na	na	0.1	na	na	0.6
2002-03	37.8	36.3	1.6	na	na	-0.1	na	na	1.6
2003-04(e)	37.3	36.4	0.8	na	na	-0.3	na	na	0.5
2004-05(e)	**36.5**	**35.9**	**0.6**	**na**	**na**	**na**	**na**	**na**	**na**
2005-06(p)	35.9	35.4	0.5	na	na	na	na	na	na
2006-07(p)	35.6	34.8	0.7	na	na	na	na	na	na

(a) Accrual time series data are being reviewed by the ABS, in consultation with all Treasuries in 2004, as accrual reporting is now established in all jurisdictions. This should result in improved quality in time series data, and may result in some changes to these series.
(e) Estimates.
(p) Projections.
na Data not available.

Table A2: Non-financial public sector cash surplus by level of government as a per cent of GDP[(a)]

	Australian Government	State/local	Consolidated
1987-88	0.9	-1.2	-0.4
1988-89	1.8	-0.2	1.6
1989-90	0.4	-0.7	-0.4
1990-91	-0.4	-0.7	-1.2
1991-92	-2.8	-1.0	-3.8
1992-93	-4.0	-0.4	-4.3
1993-94	-3.5	0.4	-3.0
1994-95	-2.4	0.4	-2.0
1995-96	-2.1	0.7	-1.4
1996-97	-0.9	0.8	-0.1
1997-98	0.4	0.7	1.1
1998-99	0.7	-1.2	-0.5
1999-00	1.7	0.8	2.4
2000-01	0.9	0.3	1.3
2001-02	0.0	0.6	0.6
2002-03	1.2	0.4	1.6
2003-04(e)	0.7	-0.2	0.5
2004-05(e)	**0.5**	**na**	**na**

(a) Accrual time series data are being reviewed by the ABS, in consultation with all Treasuries in 2004, as accrual reporting is now established in all jurisdictions. This should result in improved quality in time series data, and may result in some changes to these series.

(e) Estimates.

na Data not available.

Table A3: General government net interest payments by level of government[(a)]

	Australian Government(b)		State/local	
	$m	Per cent of GDP	$m	Per cent of GDP
1972-73	-266	-0.6	449	0.9
1973-74	-306	-0.5	451	0.8
1974-75	-267	-0.4	474	0.7
1975-76	-389	-0.5	526	0.7
1976-77	-161	-0.2	555	0.6
1977-78	-106	-0.1	582	0.6
1978-79	126	0.1	609	0.5
1979-80	290	0.2	634	0.5
1980-81	444	0.3	801	0.5
1981-82	475	0.3	785	0.5
1982-83	654	0.4	1,034	0.6
1983-84	1,327	0.6	1,347	0.7
1984-85	2,462	1.1	1,405	0.6
1985-86	3,626	1.5	1,159	0.5
1986-87	4,387	1.6	1,493	0.5
1987-88	4,019	1.3	2,127	0.7
1988-89	3,722	1.1	2,158	0.6
1989-90	3,848	1.0	3,153	0.8
1990-91	2,834	0.7	3,364	0.8
1991-92	2,739	0.7	4,397	1.1
1992-93	2,912	0.7	4,901	1.1
1993-94	4,549	1.0	4,771	1.1
1994-95	6,310	1.3	4,182	0.9
1995-96	7,812	1.6	3,636	0.7
1996-97	8,449	1.6	2,515	0.5
1997-98	7,381	1.3	1,617	0.3
1998-99	6,901	1.2	1,633	0.3
1999-00	6,014	1.0	134	0.0
2000-01	4,855	0.7	187	0.0
2001-02	4,238	0.6	1,402	0.2
2002-03	3,641	0.5	625	0.1
2003-04(e)	2,980	0.4	672	0.1
2004-05(e)	**2,873**	**0.3**	**na**	**na**
2005-06(p)	3,820	0.4	na	na
2006-07(p)	2,560	0.3	na	na
2007-08(p)	1,401	0.1	na	na

(a) Accrual time series data are being reviewed by the ABS, in consultation with all Treasuries in 2004, as accrual reporting is now established in all jurisdictions. This should result in improved quality in time series data, and may result in some changes to these series.
(b) There is a break in the Australian Government net debt and net interest payments series between 1998-99 and 1999-2000 (the first year of accrual budgeting). Up to 1998-99, Australian Government debt instruments are valued at historic cost. From 1999-2000 onwards, Australian Government debt instruments are valued at market prices, consistent with accrual Government Finance Statistics (GFS) standards.
(e) Estimates.
(p) Projections.
na Data not available.

Table A4: Non-financial public sector net debt[(a)(b)]

	General government						PNFCs		Non-financial public sector	
	Australian Government		State/local		Consolidated		Consolidated		Consolidated	
	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP
1987-88	27,359	8.8	24,201	7.8	46,410	14.9	55,293	17.8	101,703	32.7
1988-89	21,982	6.2	21,683	6.2	39,232	11.1	56,363	16.0	95,595	27.2
1989-90	16,121	4.2	27,672	7.2	37,989	9.9	57,794	15.0	95,783	24.9
1990-91	16,936	4.3	31,322	7.9	41,380	10.4	60,745	15.3	102,125	25.7
1991-92	31,132	7.7	39,167	9.6	63,525	15.6	59,011	14.5	122,536	30.1
1992-93	55,218	13.0	44,020	10.3	94,048	22.1	52,878	12.4	146,926	34.5
1993-94	70,223	15.7	40,693	9.1	106,439	23.8	48,021	10.7	154,460	34.6
1994-95	83,492	17.7	37,039	7.9	117,973	25.0	46,482	9.9	164,455	34.9
1995-96	95,831	19.1	24,981	5.0	118,053	23.5	40,135	8.0	158,188	31.5
1996-97	96,281	18.2	19,757	3.7	113,236	21.4	37,748	7.1	150,984	28.5
1997-98	82,935	14.8	15,937	2.8	95,122	16.9	35,371	6.3	130,493	23.3
1998-99	70,402	11.9	14,367	2.4	80,787	13.6	34,433	5.8	115,219	19.5
1999-00	53,768	8.6	7,885	1.3	57,647	9.2	39,334	6.3	96,981	15.5
2000-01	42,651	6.4	1,703	0.3	40,125	6.0	43,957	6.5	84,082	12.5
2001-02	38,024	5.3	-4,280	-0.6	29,539	4.1	43,461	6.1	73,001	10.2
2002-03	29,665	3.9	-9,757	-1.3	15,519	2.1	44,185	5.9	59,703	7.9
2003-04(e)	26,024	3.2	-11,704	-1.4	9,711	1.2	46,539	5.7	56,250	6.9
2004-05(e)	**24,696**	**2.9**	**-13,327**	**-1.6**	**6,527**	**0.8**	**na**	**na**	**na**	**na**
2005-06(p)	22,289	2.5	-15,821	-1.7	1,380	0.2	na	na	na	na
2006-07(p)	7,435	0.8	-18,557	-1.9	-16,471	-1.7	na	na	na	na
2007-08 (p)	-8,306	-0.8	na	na	na	na	na	na	na	na

(a) Between 1997-98 and 1999-2000 there is a structural shift in the net debt series as jurisdictions moved from the cash GFS framework to the accrual GFS framework. Consistent with this framework, some jurisdictions value net debt at market prices, while other jurisdictions continue to value net debt at historic cost. Australian Government net debt is valued at market prices from 1999-2000.

(b) Accrual time series data are being reviewed by the ABS, in consultation with all Treasuries in 2004, as accrual reporting is now established in all jurisdictions. This should result in improved quality in time series data, and may result in some changes to these series.

(e) Estimates.

(p) Projections.

na Data not available.

APPENDIX B: DATA

The information in this Statement is consistent with the Australian Bureau of Statistics (ABS) GFS reporting framework for the public sector.

Data are presented both by level of government and institutional sector. 'Level of government' refers to the distinction between the Australian and state/local governments. When combined, the Australian and state/local governments and universities are referred to as the 'consolidated public sector'.

The clear policy intent of the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations* is that the GST is collected by the Australian Taxation Office, as an agent for the States, and appropriated to the States. The Australian Government accrual revenue and expenses and cash receipts and payments measures included in this Statement therefore differ from ABS GFS measures by treating the GST revenue as state tax revenue.

Data are sourced from the ABS *1997-98 Government Finance Statistics* (Cat. No. 5512.0) and *2002-03 Government Finance Statistics* (Cat. No. 5512.0), Australian Government Final Budget Outcomes and jurisdictions' 2003-04 mid-year reports or 2004-05 Budgets (for Victoria, Western Australia and the Australian Capital Territory). Accrual time series data are being reviewed by the ABS, in consultation with all Treasuries in 2004, as accrual reporting is now established in all jurisdictions. This should result in improved quality in time series data, and may result in some changes to these series.

Since the move to accrual budget reporting, cash surplus data from the cash flow statements are used. Cash receipts are now proxied by receipts from operating activities and sales of non-financial assets, and cash payments are proxied by payments for operating activities, purchases of non-financial assets and acquisitions of assets under finance leases. Due to methodological and data source changes associated with the move to an accrual accounting framework, time series data that use measures derived under both cash and accrual accounting should be used with caution.

Consistent with the revised GFS treatment announced by the ABS (ABS Cat. No. 5501.0, released October 2002), the Australian Government general government surplus measures in this Statement, from 1998-99 onwards, incorporate the interest component of superannuation related payments by the Australian Government general government sector in respect of accumulated public non-financial corporations superannuation liabilities.

Net debt data are sourced from the ABS *1998 Public Sector Financial Assets and Liabilities* (ABS Cat. No. 5513.0), the ABS *1999-2000 Government Finance Estimates* (ABS Cat. No. 5501.0), *2002-03 Government Finance Statistics* (Cat. No. 5512.0) and Australian Government *Budget Paper No. 1*, *Budget Strategy and Outlook 2004-05*, Statement 13. Net debt numbers from 2003-04 are taken from jurisdictions' 2003-04 mid-year reports, 2004-05 budgets and Australian Government Treasury estimates.

Australian Government budget aggregates, including net debt for 1999-2000 onwards, have been revised relative to the *2002-03 Mid-Year Economic and Fiscal Outlook* and the respective Final Budget Outcomes to incorporate changes associated with the market valuation of net debt.

PART 6
HISTORICAL AUSTRALIAN GOVERNMENT DATA

This part reports historical data for the Australian Government fiscal aggregates across the general government, public non-financial corporation and non-financial public sectors.

STATEMENT 13: HISTORICAL AUSTRALIAN GOVERNMENT DATA

This statement reports historical data for the Australian Government fiscal aggregates across the general government, public non-financial corporations and non-financial public sectors.

STATEMENT 13: HISTORICAL AUSTRALIAN GOVERNMENT DATA

Statement 13 provides historical data for the Australian Government fiscal aggregates across the general government, public non-financial corporations and non-financial public sectors.

Under the accrual Government Finance Statistics (GFS) framework, flows are recorded in the period in which they occurred. As a result, prior period outcomes may be revised where information arises that could reasonably be expected to have been known in the past, is material in at least one of the affected periods and can be reliably assigned to the relevant period(s).

Estimates up to and including 1998-99 are calculated on cash terms, while estimates from 1999-2000 onwards are derived from an accrual framework. Due to methodological and data-source changes associated with the move to an accrual accounting framework, time series data that include measures derived under both cash and accrual accounting should be used with caution.

There are other structural breaks within the data set, prior to the shift to accrual reporting. Classification differences and revisions, as well as changes to the structure of the budget, can impact on comparisons over such an extended period.

Specific factors that affect the comparability of data between years include:

- classification differences in the data relating to the period prior to 1976-77 (which means that earlier data may not be entirely consistent with data for 1976-77 onwards);
- adjustments in the coverage of agencies included in the accounts of the different sectors. These include the reclassification of Central Banking Authorities from the general government to the public financial corporations sector in 1998-99, and subsequent backcasting to account for this change;
- consistent with the revised GFS treatment announced by the Australian Bureau of Statistics (ABS) (Cat. No. 5501.0, released October 2002), the general government surplus measures in this statement, from 1998-99 onwards, incorporate the interest component of superannuation related payments by the Australian Government general government in respect of accumulated public non-financial corporations' superannuation liabilities;
- transfers of taxing powers between the Australian Government and the States;
- other changes in financial arrangements between the Australian Government and the State/local government sector; and

- changes in arrangements for transfer payments, where tax concessions or rebates are replaced by payments through the social security system. This has the effect of increasing both cash receipts and payments, as compared with earlier periods, but not changing cash balances. Changes in the opposite direction (tax expenditures replacing payments) reduce both cash payments and receipts.

While approximate adjustments can be made to identify trends in budget aggregates on a generally consistent basis, the further back the analysis is taken, the more difficult the task becomes.

Table 1: Australian Government general government sector receipts, payments and surplus[(a)]

	Receipts			Payments			Cash surplus	
	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP	$m	Per cent of GDP
1970-71	8,000	6.0	20.9	7,176	10.0	18.7	824	2.1
1971-72	8,827	3.3	20.9	7,987	4.2	18.9	840	2.0
1972-73	9,414	0.4	19.8	9,120	7.5	19.2	294	0.6
1973-74	11,890	10.4	20.6	10,829	3.8	18.8	1,061	1.8
1974-75	15,325	5.8	22.6	15,275	15.8	22.5	50	0.1
1975-76	18,316	3.6	23.0	19,876	12.8	25.0	-1,560	-2.0
1976-77	21,418	4.2	23.3	22,657	1.6	24.7	-1,239	-1.4
1977-78	23,491	0.9	23.4	25,489	3.5	25.4	-1,998	-2.0
1978-79	25,666	3.0	22.6	27,753	2.7	24.5	-2,087	-1.8
1979-80	29,780	5.9	23.1	31,041	2.1	24.1	-1,261	-1.0
1980-81	35,148	6.9	24.1	35,260	2.9	24.2	-112	-0.1
1981-82	40,831	2.9	24.3	40,394	1.4	24.0	437	0.3
1982-83	44,675	-1.7	24.7	47,907	6.5	26.5	-3,232	-1.8
1983-84	49,102	2.9	24.0	55,966	9.4	27.4	-6,864	-3.4
1984-85	57,758	11.8	25.6	63,639	8.1	28.2	-5,881	-2.6
1985-86	64,845	5.8	26.1	69,838	3.4	28.1	-4,993	-2.0
1986-87	73,145	5.3	26.9	75,392	0.8	27.7	-2,247	-0.8
1987-88	81,217	3.4	26.1	79,440	-1.8	25.6	1,777	0.6
1988-89	88,369	0.4	25.1	82,202	-4.5	23.4	6,167	1.8
1989-90	95,517	1.8	24.8	88,882	1.8	23.1	6,635	1.7
1990-91	97,705	-2.4	24.6	97,333	4.5	24.5	372	0.1
1991-92	92,966	-6.8	22.9	104,551	5.2	25.7	-11,585	-2.8
1992-93	94,448	0.5	22.2	111,484	5.5	26.2	-17,036	-4.0
1993-94	100,142	5.1	22.4	117,252	4.2	26.2	-17,110	-3.8
1994-95	109,720	8.7	23.3	122,901	4.0	26.1	-13,181	-2.8
1995-96	121,105	7.6	24.1	131,182	4.0	26.1	-10,077	-2.0
1996-97	129,845	5.1	24.5	135,126	1.0	25.5	-5,281	-1.0
1997-98	135,779	3.1	24.2	134,608	-1.8	24.0	1,171	0.2
1998-99	146,496	7.4	24.7	142,159	5.1	24.0	4,337	0.7
1999-00	165,806	na	26.5	152,747	na	24.4	13,059	2.1
2000-01	160,829	-7.2	24.0	154,858	-3.0	23.1	5,970	0.9
2001-02	162,524	-0.9	22.8	163,507	3.5	22.9	-983	-0.1
2002-03	176,147	5.6	23.4	168,661	0.5	22.4	7,486	1.0
2003-04(e)	185,214	1.2	22.8	180,629	3.0	22.3	4,586	0.6
2004-05(e)	**194,237**	**2.3**	**22.6**	**191,846**	**3.6**	**22.3**	**2,391**	**0.3**
2005-06(p)	201,831	1.9	22.3	200,244	2.4	22.1	1,587	0.2
2006-07(p)	211,832	2.9	22.1	208,394	2.1	21.8	3,438	0.4
2007-08(p)	222,748	3.1	22.1	218,247	2.7	21.6	4,501	0.4

(a) There is a break in the series between 1998-99 and 1999-2000. Data for the years up to and including 1998-99 are consistent with the cash ABS GFS reporting requirements. From 1999-2000 onwards, data are derived from an accrual ABS GFS reporting framework, with receipts proxied by receipts from operating activities and sales of non-financial assets, and payments proxied by payments for operating activities, purchases of non-financial assets and net acquisition of assets under finance leases. Due to associated methodological and data-source changes, time series data that encompass measures derived under both cash and accrual accounting should be used with caution.

na Not applicable, due to a structural break in the series.

Table 2: Australian Government general government sector taxation receipts, non-taxation receipts and total receipts[(a)]

	Taxation receipts			Non-taxation receipts			Total receipts		
	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP
1970-71	7,148	6.0	18.6	852	6.0	2.2	8,000	6.0	20.9
1971-72	7,887	3.3	18.6	940	3.2	2.2	8,827	3.3	20.9
1972-73	8,411	0.4	17.7	1,003	0.4	2.1	9,414	0.4	19.8
1973-74	10,832	12.6	18.8	1,058	-7.8	1.8	11,890	10.4	20.6
1974-75	14,141	7.2	20.8	1,184	-8.1	1.7	15,325	5.8	22.6
1975-76	16,920	3.7	21.3	1,396	2.2	1.8	18,316	3.6	23.0
1976-77	19,714	3.8	21.5	1,704	8.7	1.9	21,418	4.2	23.3
1977-78	21,428	0.0	21.4	2,063	11.3	2.1	23,491	0.9	23.4
1978-79	23,409	3.0	20.6	2,257	3.2	2.0	25,666	3.0	22.6
1979-80	27,473	7.1	21.3	2,307	-6.7	1.8	29,780	5.9	23.1
1980-81	32,641	7.6	22.4	2,507	-1.5	1.7	35,148	6.9	24.1
1981-82	37,880	2.7	22.5	2,951	4.2	1.8	40,831	2.9	24.3
1982-83	41,025	-2.7	22.7	3,650	11.1	2.0	44,675	-1.7	24.7
1983-84	44,849	2.4	21.9	4,253	9.1	2.1	49,102	2.9	24.0
1984-85	52,970	12.3	23.5	4,788	7.0	2.1	57,758	11.8	25.6
1985-86	58,841	4.7	23.7	6,004	18.2	2.4	64,845	5.8	26.1
1986-87	66,467	5.5	24.4	6,678	3.9	2.5	73,145	5.3	26.9
1987-88	75,076	5.2	24.2	6,141	-14.3	2.0	81,217	3.4	26.1
1988-89	83,452	2.6	23.7	4,917	-26.1	1.4	88,369	0.4	25.1
1989-90	90,773	2.4	23.6	4,744	-9.1	1.2	95,517	1.8	24.8
1990-91	92,739	-2.5	23.3	4,966	-0.1	1.2	97,705	-2.4	24.6
1991-92	87,364	-7.7	21.5	5,602	10.5	1.4	92,966	-6.8	22.9
1992-93	88,760	0.5	20.8	5,688	0.4	1.3	94,448	0.5	22.2
1993-94	93,362	4.2	20.9	6,780	18.1	1.5	100,142	5.1	22.4
1994-95	104,921	11.5	22.3	4,799	-29.8	1.0	109,720	8.7	23.3
1995-96	115,700	7.5	23.0	5,405	9.8	1.1	121,105	7.6	24.1
1996-97	124,559	5.5	23.5	5,286	-4.1	1.0	129,845	5.1	24.5
1997-98	130,984	3.7	23.3	4,795	-10.6	0.9	135,779	3.1	24.2
1998-99	141,105	7.2	23.8	5,391	11.9	0.9	146,496	7.4	24.7
1999-00	150,695	na	24.1	15,111	na	2.4	165,806	na	26.5
2000-01	146,056	-7.3	21.8	14,774	-6.4	2.2	160,829	-7.2	24.0
2001-02	147,544	-1.0	20.7	14,980	-0.6	2.1	162,524	-0.9	22.8
2002-03	160,661	6.1	21.3	15,487	0.7	2.1	176,147	5.6	23.4
2003-04(e)	170,544	2.1	21.0	14,671	-8.9	1.8	185,214	1.2	22.8
2004-05(e)	**179,663**	**2.7**	**20.9**	**14,574**	**-3.1**	**1.7**	**194,237**	**2.3**	**22.6**
2005-06(p)	187,480	2.3	20.7	14,351	-3.4	1.6	201,831	1.9	22.3
2006-07(p)	197,381	3.3	20.6	14,451	-1.2	1.5	211,832	2.9	22.1
2007-08(p)	207,864	3.3	20.6	14,884	1.0	1.5	222,748	3.1	22.1

(a) There is a break in the series between 1998-99 and 1999-2000. Data for the years up to and including 1998-99 are consistent with the cash ABS GFS reporting requirements. From 1999-2000 onwards, data are derived from an accrual ABS GFS reporting framework, with receipts proxied by receipts from operating activities and sales of non-financial assets, and payments proxied by payments for operating activities, purchases of non-financial assets and net acquisition of assets under finance leases. Due to associated methodological and data-source changes, time series data that encompass measures derived under both cash and accrual accounting should be used with caution.

na Not applicable, due to a structural break in the series.

Table 3: Australian Government general government sector net debt and net interest payments[(a)]

	Net debt(b)		Net interest payments(c)	
	$m	Per cent of GDP	$m	Per cent of GDP
1972-73	-790	-1.7	-266	-0.6
1973-74	-1,851	-3.2	-306	-0.5
1974-75	-1,901	-2.8	-267	-0.4
1975-76	-341	-0.4	-389	-0.5
1976-77	898	1.0	-161	-0.2
1977-78	2,896	2.9	-106	-0.1
1978-79	4,983	4.4	126	0.1
1979-80	6,244	4.8	290	0.2
1980-81	6,356	4.4	444	0.3
1981-82	5,919	3.5	475	0.3
1982-83	9,151	5.1	654	0.4
1983-84	16,015	7.8	1,327	0.6
1984-85	21,896	9.7	2,462	1.1
1985-86	26,889	10.8	3,626	1.5
1986-87	29,136	10.7	4,387	1.6
1987-88	27,359	8.8	4,019	1.3
1988-89	21,982	6.2	3,722	1.1
1989-90	16,121	4.2	3,848	1.0
1990-91	16,936	4.3	2,834	0.7
1991-92	31,132	7.7	2,739	0.7
1992-93	55,218	13.0	2,912	0.7
1993-94	70,223	15.7	4,549	1.0
1994-95	83,492	17.7	6,310	1.3
1995-96	95,831	19.1	7,812	1.6
1996-97	96,281	18.2	8,449	1.6
1997-98	82,935	14.8	7,381	1.3
1998-99	70,402	11.9	6,901	1.2
1999-00	53,768	8.6	6,014	1.0
2000-01	42,651	6.4	4,855	0.7
2001-02	38,024	5.3	4,238	0.6
2002-03	29,665	3.9	3,641	0.5
2003-04(e)	26,024	3.2	2,980	0.4
2004-05(e)	**24,696**	**2.9**	**2,873**	**0.3**
2005-06(p)	22,289	2.5	3,820	0.4
2006-07(p)	7,435	0.8	2,560	0.3
2007-08(p)	-8,306	-0.8	1,401	0.1

(a) There is a break in the net debt and net interest series between 1998-99 and 1999-2000 (the first year of accrual budgeting). Up to 1998-99, Australian Government general government debt instruments are valued at historic cost. From 1999-2000 onwards, Australian Government general government debt instruments are valued at market prices, consistent with accrual GFS standards.

(b) Source: ABS Cat. No. 5501.0, 5513.0, Australian Government Final Budget Outcomes and Treasury estimates.

(c) Excludes superannuation related interest flows.

Table 4: Australian Government general government sector revenue, expenses, net capital investment, fiscal balance and net worth[(a)]

	Revenue		Expenses		Net capital investment		Fiscal balance		Net worth(b)(c)	
	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP
1996-97	141,688	26.7	145,809	27.5	90	0.0	-4,211	-0.8	-74,354	-14.0
1997-98	146,820	26.2	148,646	26.5	147	0.0	-1,973	-0.4	-68,544	-12.2
1998-99	151,897	25.7	146,620	24.8	1,433	0.2	3,844	0.6	-76,150	-12.9
1999-00	166,595	26.6	154,481	24.7	-1,225	-0.2	13,339	2.1	-39,105	-6.2
2000-01	161,508	24.1	156,817	23.4	-1,168	-0.2	5,859	0.9	-41,769	-6.2
2001-02	162,370	22.7	166,525	23.3	-369	-0.1	-3,786	-0.5	-47,553	-6.7
2002-03	175,014	23.2	169,247	22.4	-219	0.0	5,986	0.8	-51,333	-6.8
2003-04(e)	186,197	23.0	183,136	22.6	18	0.0	3,044	0.4	-43,545	-5.4
2004-05(e)	**193,151**	**22.5**	**192,306**	**22.4**	**148**	**0.0**	**698**	**0.1**	**-42,836**	**-5.0**
2005-06(p)	201,383	22.2	200,626	22.1	45	0.0	712	0.1	-42,926	-4.7
2006-07(p)	212,199	22.2	210,033	22.0	-125	0.0	2,291	0.2	-38,515	-4.0
2007-08(p)	223,129	22.1	220,939	21.9	-429	0.0	2,619	0.3	-37,434	-3.7

(a) The fiscal balance is equal to revenue less expenses less net capital investment. Net worth is calculated as assets less liabilities.
(b) There is a break in the net worth series between 1998-99 and 1999-2000. Data up to 1998-99 are sourced from the Australian Government's Consolidated Financial Statements based on Australian accounting standards. Data beginning in 1999-2000 are based on the GFS framework. For the general government sector, the major change across the break in the series is an improvement in net worth. This is primarily due to the move from valuing investments in public corporations at historic cost to current market value (which is calculated using the share price for listed corporations). This is partly offset by defence weapons platforms no longer being recorded as assets and valuing debt at current market value.
(c) Following advice from the ABS, the net worth series has been revised back to 1999-2000 to remove dividends payable from the measurement of the general government sector's equity holding in the public financial corporations sector. From 2002-03 net worth also includes the initial recognition of a provision for asbestos related claims. At the time of the 2002-03 Final Budget Outcome a reliable actuarial measure was not available. Following an actuarial review a provision for asbestos related claims was included in the audited 2002-03 Consolidated Financial Statements.

Table 5: Australian Government general government sector accrual taxation revenue, non-taxation revenue and total revenue

	Taxation revenue			Non-taxation revenue			Total revenue		
	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP
1999-00	152,576	na	24.4	14,020	na	2.2	166,595	na	26.6
2000-01	151,156	-5.2	22.5	10,352	-29.3	1.5	161,508	-7.2	24.1
2001-02	149,848	-2.8	21.0	12,522	18.6	1.8	162,370	-1.4	22.7
2002-03	163,055	6.0	21.6	11,958	-7.0	1.6	175,014	5.0	23.2
2003-04(e)	174,082	2.7	21.5	12,115	-2.5	1.5	186,197	2.4	23.0
2004-05(e)	**182,580**	**2.3**	**21.3**	**10,571**	**-14.9**	**1.2**	**193,151**	**1.2**	**22.5**
2005-06(p)	190,377	2.3	21.0	11,006	2.1	1.2	201,383	2.3	22.2
2006-07(p)	200,565	3.3	21.0	11,635	3.7	1.2	212,199	3.3	22.2
2007-08(p)	211,142	3.3	20.9	11,987	1.0	1.2	223,129	3.1	22.1

na Data not available.

Table 6: Australian Government cash receipts, payments and surplus by institutional sector ($m)[(a)]

	General government			Public non-financial corporations			Non-financial public sector		
	Receipts	Payments	Cash surplus	Receipts	Payments	Cash surplus	Receipts	Payments	Cash surplus
1987-88	81,217	79,440	1,777	4,129	5,006	944	84,333	83,439	2,721
1988-89	88,369	82,202	6,167	4,177	6,035	257	91,544	87,188	6,424
1989-90	95,517	88,882	6,635	3,926	11,322	-5,261	98,387	99,081	1,374
1990-91	97,705	97,333	372	4,804	9,351	-2,139	101,315	105,476	-1,767
1991-92	92,966	104,551	-11,585	3,899	7,713	101	95,063	110,448	-11,484
1992-93	94,448	111,484	-17,036	4,385	7,819	-196	97,327	117,775	-17,232
1993-94	100,142	117,252	-17,110	5,178	6,476	1,482	103,065	121,457	-15,628
1994-95	109,720	122,901	-13,181	5,262	7,318	1,956	113,013	128,247	-11,225
1995-96	121,105	131,182	-10,077	4,927	8,190	-527	123,269	136,607	-10,604
1996-97	129,845	135,126	-5,281	4,782	7,373	473	131,512	139,385	-4,808
1997-98	135,779	134,608	1,171	6,238	7,923	1,119	139,560	140,006	2,290
1998-99	146,496	142,159	4,337	na	na	-353	na	na	3,984
1999-00	165,806	152,747	13,059	na	na	-2,594	na	na	10,465
2000-01	160,829	154,858	5,970	na	na	391	na	na	6,362
2001-02	162,524	163,507	-983	na	na	1,210	na	na	227
2002-03	176,147	168,661	7,486	na	na	1,280	na	na	8,766
2003-04(e)	185,214	180,629	4,586	na	na	1,199	na	na	5,785
2004-05(e)	**194,237**	**191,846**	**2,391**	**na**	**na**	**2,212**	**na**	**na**	**4,603**
2005-06(p)	201,831	200,244	1,587	na	na	na	na	na	na
2006-07(p)	211,832	208,394	3,438	na	na	na	na	na	na
2007-08(p)	222,748	218,247	4,501	na	na	na	na	na	na

(a) There is a break in the series between 1998-99 and 1999-2000. Data for the years up to and including 1998-99 are consistent with the cash ABS GFS reporting requirements. From 1999-2000 onwards, data are derived from an accrual ABS GFS reporting framework, with receipts proxied by receipts from operating activities and sales of non-financial assets, and payments proxied by payments for operating activities, purchases of non-financial assets and net acquisition of assets under finance leases. Due to associated methodological and data-source changes, time series data which encompasses measures derived under both cash and accrual accounting should be used with caution.

na Data not available.

Table 7: Australian Government accrual revenue, expenses and fiscal balance by institutional sector[(a)]

	General government			Public non-financial corporations			Non-financial public sector		
	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance
1996-97	141,688	145,809	-4,211	27,431	26,015	-331	na	na	-4,542
1997-98	146,820	148,646	-1,973	29,618	26,999	2,360	na	na	387
1998-99	151,897	146,620	3,844	27,687	26,088	-816	175,682	168,806	3,028
1999-00	166,595	154,481	13,339	25,270	23,327	1,062	188,347	173,134	14,400
2000-01	161,508	156,817	5,859	25,640	24,533	-826	183,000	177,202	5,034
2001-02	162,370	166,525	-3,786	26,461	25,164	793	184,577	187,435	-2,993
2002-03	175,014	169,247	5,986	24,172	22,750	1,975	194,391	187,244	7,919
2003-04(e)	186,197	183,136	3,044	24,893	23,787	1,752	206,427	202,259	4,795
2004-05(e)	**193,151**	**192,306**	**698**	**25,757**	**23,338**	**2,535**	**214,567**	**211,302**	**3,233**
2005-06(p)	201,383	200,626	712	na	na	na	na	na	na
2006-07(p)	212,199	210,033	2,291	na	na	na	na	na	na
2007-08(p)	223,129	220,939	2,619	na	na	na	na	na	na

(a) The fiscal balance is equal to revenue less expenses less net capital investment. Net capital investment is not shown in this table.
na Data not available.

INDEX

C

D

E

F

G

S

T

U