2005-06 BUDGET PAPER No. 1

BUDGET STRATEGY AND OUTLOOK 2005-06

CIRCULATED BY
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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 (GDP) deflator;
- the budget year refers to 2005-06, while the forward years refer to 2006-07, 2007-08 and 2008-09; 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
-	nil
na	not applicable (unless otherwise specified)
(e)	estimates (unless otherwise specified)
(p)	projections (unless otherwise specified)
$m	$ million
$b	$ billion

(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	Victoria
QLD	Queensland
WA	Western Australia
SA	South Australia
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 2005-06 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.

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PART 1
FISCAL STRATEGY AND BUDGET PRIORITIES

This part provides an overview of the fiscal and economic outlook, describes the government's fiscal strategy and outlines the key budget priorities.

Statement 1: Fiscal Strategy and Budget Priorities

Australia's strong economic performance and fiscal management continues to be amongst the best in the developed world. The 2005-06 Budget puts in place major initiatives to sustain this performance, including further income tax cuts and welfare to work reforms, while maintaining strong budget surpluses over the next four years. These initiatives will boost participation in the workforce and increase the productive capacity of the economy over time, thereby enhancing Australia's growth prospects and its capacity to deal with future demographic pressures in a sustainable way.

In this budget the Government will introduce personal income tax cuts worth $21.7 billion over four years, improving the incentives for all Australian taxpayers to participate in the workforce. The superannuation surcharge will be abolished at a cost of $2.5 billion over four years, increasing incentives to save and boosting retirement incomes.

Substantive reform of the income support system for people of workforce age will encourage greater workforce participation by those with capacity to work. Obligations to look for work will be applied to a wider range of people, the payment structure will be altered to encourage participation and extra services will be provided to help people to prepare for and stay in work.

The Government will abolish the Tariff Concession Scheme, at a cost of $1.25 billion over four years, as well as provide other business tax relief aimed at enhancing business investment and Australia's international competitiveness.

This budget also includes measures to address the fiscal sustainability of the health system, particularly through changes to the Medicare Safety Net and the Pharmaceutical Benefits Scheme.

The Australian economy is forecast to continue to grow solidly, with GDP growth forecast to strengthen from around 2 per cent in 2004-05 to 3 per cent in 2005-06. With unemployment at a 28-year low, the economy is set to deliver sustained improvements in Australia's economic wellbeing.

Having met the need for spending in priority areas, an underlying cash surplus of $8.9 billion is expected in 2005-06, with further surpluses projected for the 3 years following.

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STATEMENT 1: FISCAL STRATEGY AND BUDGET PRIORITIES

FISCAL OUTLOOK

The fiscal outlook for Australia remains very strong, with the Government forecasting its eighth budget surplus. Australia is in a much stronger fiscal position than most comparable economies.

The 2005-06 Budget puts in place a series of major initiatives aimed at sustaining Australia's economic performance, including income tax cuts and the abolition of the Tariff Concession Scheme. The budget also introduces welfare to work reforms which will boost participation in the workforce, increase the productive capacity of the economy and strengthen Australia's fiscal position in preparation for the ageing of the population. The budget outlines arrangements for a Future Fund to make a provision for unfunded liabilities the nation faces, easing the cost of future demographic change.

An underlying cash surplus of $8.9 billion is expected in 2005-06 compared with an estimated surplus of $4.5 billion at the *Mid Year Economic and Fiscal Outlook 2004-05* (MYEFO). Underlying cash surpluses continue to be projected across the forward estimates.

Table 1: Budget aggregates

	Actual	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
Underlying cash balance ($b)(a)	**8.0**	**9.2**	**8.9**	**7.9**	**8.5**	**9.3**
Per cent of GDP	1.0	1.1	1.0	0.8	0.8	0.9
Fiscal balance ($b)	**4.8**	**7.0**	**7.4**	**7.5**	**8.0**	**9.0**
Per cent of GDP	0.6	0.8	0.8	0.8	0.8	0.9

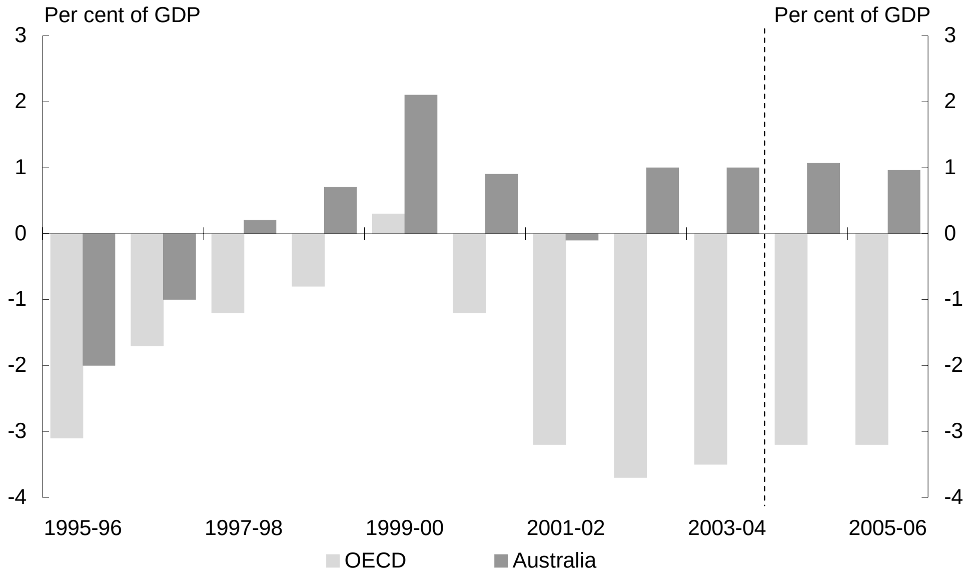
(a) Excludes expected Future Fund earnings from 2005-06 onwards. For further explanation refer to Statement 2 Box 1 and Statement 8.

Expected Future Fund earnings are excluded from the underlying cash balance. This recognises that these resources are not available for recurrent spending, instead being pre-committed to fund existing liabilities. This represents a tightening of fiscal policy.

In accrual terms, a fiscal surplus of $7.4 billion is now expected for 2005-06 compared to a surplus of $3.5 billion estimated at MYEFO.

Australia's very strong fiscal position compared to OECD countries is highlighted in Chart 1. The fiscal position amongst OECD countries, on average, is expected to remain in deficit in 2005-06 and 2006-07, notwithstanding strong global growth.

Chart 1: International comparison of budget balances



Source: OECD Economic Outlook 76 November 2004 and Budget Paper No. 1, *Budget Strategy and Outlook 2005-06*.

ECONOMIC OUTLOOK

The outlook for the Australian economy is for solid output growth, low unemployment and moderate inflation. In year-average terms, GDP growth is forecast to strengthen from around 2 per cent in 2004-05 to 3 per cent in 2005-06. Australia will continue to benefit from higher terms of trade in 2005-06. Strong world demand has resulted in substantial increases in contract prices for some of Australia's bulk commodity exports. These high export prices will result in strong growth in national income through 2005-06.

The combination of solid output growth, moderate inflation and a 28-year low in unemployment provides a sound platform for further sustained improvement in Australia's economic wellbeing.

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

	Forecasts		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
Real GDP	2	3	3 1/2	3 1/2	3 1/4
Employment(a)	2 3/4	1 3/4	1 1/2	1 1/2	1 1/4
Wages(b)	3 3/4	4	3 3/4	3 3/4	4
CPI	2 1/2	2 3/4	2 1/2	2 1/2	2 1/2

(a) Labour Force Survey.
(b) Wage Price Index.
Source: Australian Bureau of Statistics (ABS) Cat. No 5206.0, 6202.0, 6401.0, 6345.0 and Treasury.

Table 2 presents the major economic parameters used in preparing the budget. The parameters for 2004-05 and 2005-06 are forecasts while those for 2006-07, 2007-08 and 2008-09 are projections.

Projections for 2008-09 incorporate an employment growth assumption that has been adjusted down by ¼ of a percentage point. This reflects, for the first time, the anticipated decline in labour market participation as the population ages and some 'baby boomers' start to retire. The downward adjustment to employment brings projected GDP growth down to 3¼ per cent in 2008-09. Real GDP projections and updated analysis of labour force projections from the Intergenerational Report 2002-03 are discussed in Box 6 of Statement 3.

The nominal GDP projections incorporate a technical assumption that commodity prices will return progressively to their long-run average level. This technical assumption recognises the probability that present historically high commodity prices will not persist as world supply expands. The technical assumption has the effect of reducing nominal GDP growth in 2006-07 and 2007-08. Real GDP growth projections for these years are unchanged. The assumptions underlying the nominal GDP projections are discussed in more detail in Box 7 of Statement 3.

FISCAL STRATEGY

The Government's medium-term fiscal strategy is an integral part of the economic management framework designed to deliver sustainable economic growth, rising employment and higher living standards.

A medium-term approach to fiscal policy

The primary objective of the medium-term fiscal strategy is to maintain budget balance, on average, over the course of the economic cycle. This 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 budget balance over the cycle through a disciplined and prioritised approach to spending and not by recourse to increased taxation.

Central to the Government's objective of improving net worth is the establishment of the Future Fund, dedicated to funding the public sector superannuation liability — the largest liability on the balance sheet, currently valued at $91 billion. To ensure that government saving will grow sufficiently to meet future superannuation payments, expected Fund earnings are excluded from the underlying cash balance. This means that the Fund's earnings are not available for recurrent spending and will contribute to improving the Government's net worth over time.

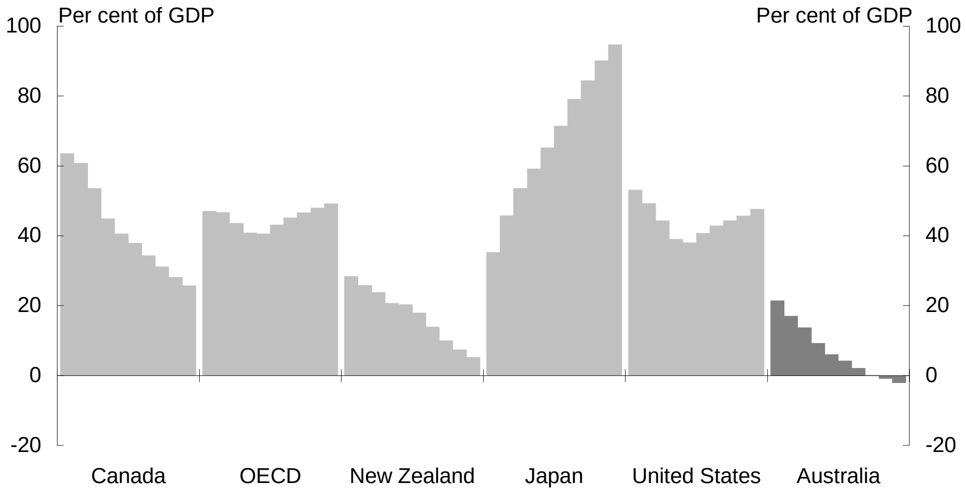
Consistent with the Government's fiscal strategy, this budget delivers another substantial surplus in 2005-06 and further surpluses over the medium term. This will help contain inflationary pressures in the economy, thus supporting a low interest rate environment, and will add to national savings.

The surplus in 2005-06 is larger than envisaged at the time of MYEFO, supported by recent unexpected increases in commodity export prices. Larger surpluses mean that the Government is saving some of the additional income Australia is earning from the rest of the world.

A decade of sound economic management has enabled Australia to make the most of its opportunities in the global economy. The Government remains committed to ensuring strong economic outcomes are sustained. It is appropriate that the Government take a prudent approach to fiscal policy, particularly as national income is currently being boosted as a result of higher commodity prices which are not expected to be permanent. This prudent approach ensures public finances will be well-positioned to meet future challenges, including those flowing from demographic change and the increasing demand for high-quality health care.

The Government has a strong record of 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 2).

Chart 2: General government net debt levels in selected countries (1997 to 2006)



Source: International data are sourced from OECD Economic Outlook 76 December 2004. Australian data are sourced from Statement 12. All data are for the total general government sector.

BUDGET STRATEGY AND PRIORITIES

The Government's budget strategy seeks to foster a prosperous and secure environment where all members of society have opportunities to contribute to the community and to share in the rewards of responsible economic management.

To ensure the Australian economy can continue to deliver sustainable economic growth, rising employment and higher living standards, this budget focuses on:

- continued responsible economic management, including strong surpluses in each of the next four years and measures to prevent costly burdens being placed on future generations (ensuring fiscal sustainability);
- increasing incentives to work and save and addressing impediments that prevent people who are capable of working from engaging in the labour market (increasing workforce participation); and
- implementing policies that increase the productive capacity of the economy (enhancing productivity).

Income tax cuts and increased funding on major health and aged care priorities will improve the wellbeing of Australians today. However, this budget also addresses the challenges to Australia's prosperity over the decades ahead.

The Government's *Intergenerational Report 2002-03* discussed how, over the next 40 years, the proportion of our population aged 65 or more will double while the population of workforce age will grow by just 14 per cent. The *Intergenerational Report 2002-03* noted that pressures in key areas of government spending — notably health, aged care and pensions — could give rise to a 'fiscal gap' of around 5 per cent of GDP in the absence of policy change.

The recent Productivity Commission report on *Economic Implications of an Ageing Australia* (March 2005) reinforced the findings of the *Intergenerational Report 2002-03*, noting that fiscal pressures arising from an ageing population will fall predominantly in areas of Australian Government, rather than State Government, responsibility. Policy responses will need to focus on enhancing both workforce participation and productivity in order to generate the economic growth needed to meet these fiscal pressures, without raising taxes as a proportion of GDP.

The demographic pressures identified in the *Intergenerational Report 2002-03* are starting to be felt during this budget period. Economic growth projections for 2008-09 have been adjusted down by one quarter of a percentage point as a result of the ageing of the population.

Further steps need to be taken now to address the demographic challenge to Australia's growth prospects. This budget makes an important contribution to preparing Australia to meet the demographic pressures we face. It does so within a continued framework of responsible fiscal management, delivering this Government's eighth budget surplus.

This budget demonstrates the Government's commitment to facilitating jobs growth, through welfare to work reforms, work incentives through tax relief for individuals and Australian businesses and funding to further build Australia's vocational skill base.

These measures build on the substantial reforms in the 2004-05 Budget which boosted retirement savings, provided substantial assistance to families, delivered tax cuts to improve the rewards from work, and made substantial investments to build longer-term capacity through support for science and innovation and investment in land transport infrastructure.

Personal income tax reform and family assistance

The Government is introducing personal income tax cuts worth $21.7 billion over four years. The tax cuts will improve the incentives for all Australian taxpayers to participate in the workforce. They will also improve the international competitiveness of Australia's personal income tax system by substantially raising the thresholds for the top two marginal tax rates.

From 1 July 2005, the following changes will be made to the personal income tax scale:

- the lowest marginal tax rate will be reduced from 17 per cent to 15 per cent; and
- the 42 per cent threshold will increase to $63,001 and the 47 per cent threshold will increase to $95,001.

From 1 July 2006, further reductions in personal income tax will be provided as follows:

- the 42 per cent threshold will increase to $70,001 and the 47 per cent threshold will increase to $125,001.

Table 3: New personal tax rates

Current tax thresholds Income range ($)	Tax rate %	New tax threshold from 1 July 2005 Income range ($)	Tax rate %	New tax thresholds from 1 July 2006 Income range ($)	Tax rate %
0 - 6,000	0	0 - 6,000	0	0 - 6,000	0
6,001 - 21,600	17	6,001 - 21,600	**15**	6,001 - 21,600	**15**
21,601 - 58,000	30	21,601 - **63,000**	30	21,601 - **70,000**	30
58,001 - 70,000	42	**63,001 - 95,000**	42	**70,001 - 125,000**	42
70,001 +	47	**95,001 +**	47	**125,001 +**	47

The reduction in the 17 per cent marginal tax rate to 15 per cent will improve the rewards from participating in the workforce for lower income earners. Moving the 42 per cent threshold up to $70,001 means more than 80 per cent of taxpayers will face a top marginal tax rate of 30 per cent or lower over the forward estimates period.

Senior Australians will also benefit. At present, senior Australians eligible for the Senior Australians Tax Offset and the low income tax offset pay no tax up to an annual income of $20,500 for singles and up to $33,612 for couples (depending on the income earned by each member of the couple). The tax cuts will lift these income levels up to $21,968 for singles and $36,494 for couples, and the Government will ensure that the offset will only phase out once income exceeds the effective tax free threshold for each single person or member of a couple. The Medicare levy thresholds that apply to senior Australians will also be increased to ensure that they do not pay the Medicare levy until they begin to incur an income tax liability.

These benefits to senior Australians are in addition to the Mature Age Worker Tax Offset announced since last budget, which provides a tax offset of up to $500 to workers 55 years of age and older, at a cost of $1.9 billion over four years from 2005-06.

These tax cuts build on the reforms delivered through *The New Tax System* (July 2000), and in the 2003-04 and 2004-05 Budgets. The combined effect of these tax reforms has been to deliver significant reductions in tax for all Australian taxpayers.

- Taxpayers earning $25,000 paid $4,521 in income tax prior to *The New Tax System* (excluding the Medicare levy) whereas taxpayers on that income will, from 1 July 2005, only pay $3,261; a reduction of around 28 per cent.

- Taxpayers on $60,000 paid $18,801 in tax prior to *The New Tax System* (excluding the Medicare levy), compared with $13,860, from 1 July 2005; a reduction of around 26 per cent.

- Taxpayers on $90,000 paid $32,902 in tax prior to *The New Tax System* (excluding the Medicare levy), whereas from 1 July 2006 they will pay only $25,260, a reduction of around 23 per cent.

Chart 3 below shows the percentage reductions in tax that have been delivered by the Government, over a range of taxable incomes.

Chart 3: Income tax savings since *The New Tax System*

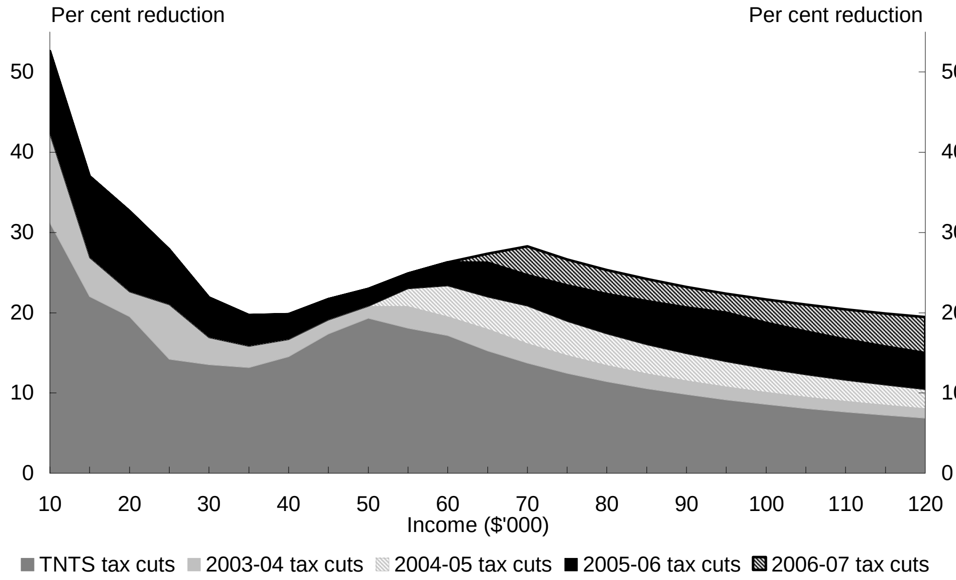
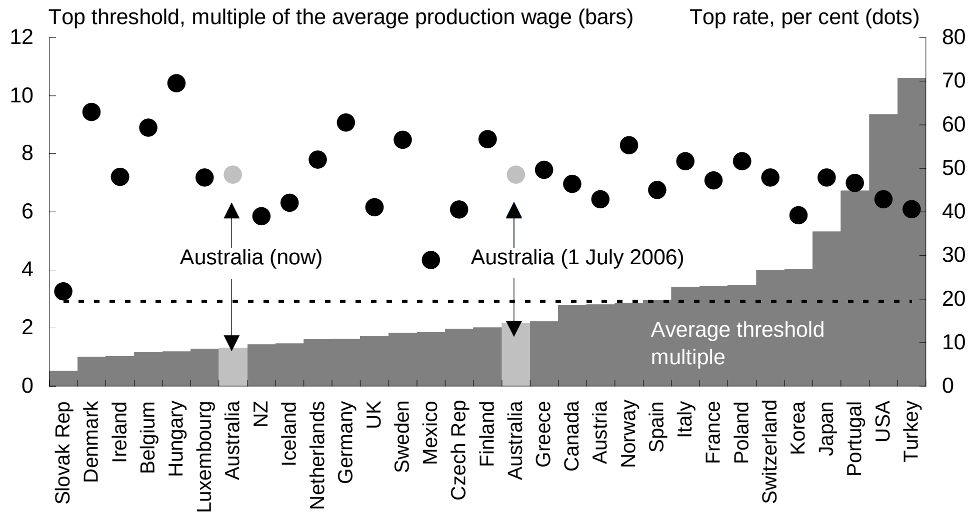


Chart 4 below shows how Australia's top income tax threshold will rise to more than twice the average production wage (a means of comparing earnings on an international basis). The substantial increase in the top threshold significantly improves Australia's position amongst the OECD countries.

Chart 4: Comparison of top tax rates and thresholds across the OECD(a)



(b) The average production wage is the full-time wage of a worker in the manufacturing sector.
Source: Based on OECD data.

From 1 July 2006, taxpayers will not face the top marginal tax rate until they earn over $125,000. This means that the top marginal tax rate will apply to only 3 per cent of taxpayers from 2006-07.

Increased assistance for families and carers

This budget also provides extra assistance for Australian families.

From 1 July 2006, the level of family income allowed before Family Tax Benefit Part A starts to be withdrawn will be increased to $37,500 a year. This will assist over 400,000 families, providing increased assistance of up to $12.55 a week.

This measure builds on the substantial increases in family assistance provided in the last budget, as well as further enhancements announced since last budget through a $300 increase in the maximum rate of Family Tax Benefit Part B, and the introduction of the 30 per cent Child Care Tax Rebate.

The Government will provide $317 million for a one-off carer bonus to be paid to eligible carers in June 2005 in recognition of their role of carer for a person with a disability. Recipients of Carer Payment will receive a $1,000 bonus payment. Recipients of Carer Allowance will receive a $600 bonus payment for each eligible care receiver. The bonus will be tax free and not treated as income when calculating social security payments.

Improving retirement incomes

The Government assists people to improve their retirement income by encouraging them to make additional voluntary superannuation contributions. In the 2004-05 Budget, the Government significantly increased the co-contribution matching rate from 100 to 150 per cent and raised the qualifying income threshold. More people are now eligible for a co-contribution. This measure has particularly benefited low and middle income earners. The maximum superannuation surcharge rate has also been gradually reduced from its original 15 per cent.

As part of this budget the superannuation surcharge will be abolished for superannuation contributions made from 1 July 2005. This will increase retirement savings for people affected by the surcharge and increase incentives to make additional contributions, at a cost of $2.5 billion over four years.

A more sustainable welfare system

This budget incorporates a comprehensive rebalancing of Australia's welfare system to make it more sustainable and to encourage increased workforce participation for those with the capacity to work. The changes recognise the importance of paid employment, whether full-time or part-time, to Australia's prosperity and each individual's own wellbeing.

More people required to look for work, and enhanced Newstart Allowance

Parents receiving Parenting Payment prior to 1 July 2006 will be able to remain on that payment under the current entitlement; that is, until their youngest child turns 16. This group of parents will have a year to seek work voluntarily from the later of 1 July 2006 or when their youngest child turns six. After that they will become subject to an obligation to seek part-time work of at least 15 hours per week.

Parents applying for Parenting Payment on or after 1 July 2006 will receive Parenting Payment while their youngest child is less than six years old. When their youngest child turns 6, this group of parents will receive enhanced Newstart and be subject to an obligation to seek part-time work of at least 15 hours per week.

The new payment and obligations arrangements

Income support recipient		Obligation	Payment
Parent, youngest child aged under 6	Existing recipient (on 30 June 2006)	None	Parenting Payment (single or partnered)
	New applicant[a] (from 1 July 2006)	None	Parenting Payment (single or partnered)
Parent, youngest child aged 6 or over	Existing recipient (on 30 June 2006)	Part-time[b]	Parenting Payment (single or partnered)
	New applicant (from 1 July 2006)	Part-time	Enhanced Newstart Allowance
Person with disabilities, capable of working 15-29 hours per week	Existing recipient (on 10 May 2005)	None	Disability Support Pension
	New applicant (11 May 2005 to 30 June 2006)	None[c]	Disability Support Pension[c]
	New applicant (from 1 July 2006)	Part-time	Enhanced Newstart Allowance

(a) When the youngest child turns 6, a part-time obligation and enhanced Newstart apply.
(b) Existing recipients of Parenting Payment have a 12 month grace period before new obligations commence, starting from the later of 1 July 2007 or their youngest child's seventh birthday.
(c) New applicants for the Disability Support Pension between 11 May 2005 and 30 June 2006 will be reassessed after 1 July 2006. If the reassessment indicates they can work 15-29 hours per week they will be placed on enhanced Newstart Allowance and have a part-time work obligation.

People in receipt of the Disability Support Pension prior to 1 July 2006 will remain on that payment with no part-time work obligation. They will be subject to the normal periodic review process for Disability Support Pension, usually every two or five years, which will apply the existing eligibility criteria (which is broadly whether that person is capable of 30 hours work per week at award wages).

People seeking to go on Disability Support Pension on or after 1 July 2006 will face new eligibility criteria. They will receive Disability Support Pension if they are assessed as being incapable of 15 hours work a week at award wages. If they are assessed as being capable of 15-29 hours work per week at award wages they will receive enhanced Newstart and be subject to an obligation to seek part-time work of at least 15 hours per week.

People applying for Disability Support Pension between 11 May 2005 and 30 June 2006 will be assessed for eligibility under the existing test; that is whether they are able to work 30 hours per week at award wages. However, their ongoing eligibility will be reassessed in periodic reviews, usually every two or five years, against the new 15-29 hours per week at award wages test, after 1 July 2006. If they are assessed as being capable of 15 hours work per week at award wages they will have an obligation to undertake part-time work and will receive enhanced Newstart.

From 1 July 2006 the Government will increase Mobility Allowance to $100 per fortnight for people with disabilities who have a part-time obligation to look for work. Disability Support Pensioners who are working 15 or more hours per week may also be eligible.

The Government will also enhance Newstart Allowance. This will support increased participation by improving the returns to part-time work. The maximum withdrawal rate will be reduced from 70 to 60 cents in the dollar. In addition, the income at which this rate commences will be increased to $250 per fortnight, up from $142 for Newstart currently. Both these changes will benefit recipients of Newstart Allowance, as well as recipients of Youth Allowance (Other), Mature Age Allowance, Widow Allowance, Sickness Allowance and Partner Allowance. Recipients of Youth Allowance (Student), Austudy and Abstudy will benefit from a reduction in the withdrawal rate from 70 cents to 60 cents in the dollar.

New and expanded services to help people get jobs

The Government will ensure that those who are obliged to look for work receive appropriate assistance to help them find work. This budget includes over $2 billion in new and expanded services to help people get jobs.

- Parents will benefit from a new $48 million Employment Preparation service, which will allow Job Network providers to purchase skills training and assessments. Employment Preparation will replace the current Transition to Work Programme.

- People with disabilities will benefit from a new $80 million Pre-Vocational Participation Account to provide limited short interventions that allow them to become job-ready quickly. Services that this will fund include pain management, work conditioning and short-term mental health interventions.

- A new Wage Assist Programme will allow Job Network providers to provide wage subsidies to employers who hire long-term unemployed people who have been making a genuine effort to find work. Wage assistance will be payable for between 13 and 26 weeks.

- A comprehensive work capacity assessment will assess all new Disability Support Pension applicants to determine whether they can work between 15 and 29 hours per week at award wages.

- An extra $266 million over four years to increase the number of child care places, including 84,300 Outside School Hours Care places.

- Other existing services will also expand. The Government will provide additional funding of: $170 million over three years for the Disability Open Employment Service programme; $178 million over three years for rehabilitation services; and $43 million over three years for additional Vocational Eduction and Training places.

A new compliance framework

The new obligations to look for work will be supported by an improved compliance framework incorporating payment suspension, rather than payment reduction. This will provide greater incentives for people to meet their obligations.

Bolstering the national skills pool

With unemployment at 5.1 per cent, its lowest level in a generation, it is not unexpected that skills shortages are emerging in some places and some sectors of the economy, particularly those benefiting from the strong terms of trade that Australia is experiencing. This budget introduces a range of initiatives in education, training and skilled migration to bolster the national skills pool.

These measures are underpinned by two longer-term drivers:

- to increase productivity by enhancing workforce skills and the capacity to apply new technologies; and

- to bolster participation, which depends vitally on educational attainment. Some 81 per cent of those of working age who have post-school qualifications are employed compared to only 61 per cent of those without such qualifications.

The Government is increasing vocational education and training (VET) places, and taking measures to attract more Australians to the rewards of a career in the trades. This budget will create 4,500 pre-vocational training places for people interested in a career in a traditional trade, at a cost of $20 million, and provide an additional 7,000 School-Based New Apprenticeships, at a cost of $26 million, so more students can begin their apprenticeships while continuing their school studies.

This budget also implements other policies announced in the recent election. Youth Allowance (as well as Austudy and Abstudy for over 25 year olds) will be extended to apprentices. 24 Australian Technical Colleges, located in areas of skill shortage and linked to industry needs will be established to provide 7,200 year 11 and 12 students with an academic and a vocational education. 20,000 New Apprenticeship Access Programme places will assist job seekers in areas of skill shortage who want a New Apprenticeship but need additional skills before they commence. Scholarships will be provided for apprentices, as well as toolkits for apprentices in skill shortage disciplines.

Through the Commonwealth-State Training Funding Agreement, over 2005 to 2008, the Government will invest a further $5 billion and deliver extra reforms which include: providing more training places in areas of skill shortage; removing impediments to user choice, so employers and employees have more freedom to choose the training organisation that best suits their needs; ensuring the system is industry-led and responds flexibly to industry needs; and providing greater access to training places and recognition of prior learning for mature workers.

The Government will continue to invest strongly in Australian schools, which underpin Australia's long-term skilled labour supply. As announced in the recent election, the Government will implement its election commitment, A Billion Dollar Investment in Our School Infrastructure. This budget also sees the Government continue the Australian Government Quality Teacher Programme at a cost of $140 million. Overall, the Government will provide $33 billion to Australian schools over 2005-2008, some $9.5 billion more than in the previous four year period.

The Government is committed to ensuring young Australians receive the guidance they need to assist them in navigating key transitions at school and the move on to further study and work. This budget will provide $143 million to deliver an Australian Network of Industry Career Advisers.

To supplement the national skills pool, the Government will increase skilled migration places by 20,000 in 2005-06 to 97,500, up from 24,100 in 1995-96, and take a range of initiatives to ensure Australia takes migrants with skills currently in short supply. In addition, it will establish a new trade skills training visa to enable overseas students to undertake apprenticeships in regional Australia on a full-fee paying basis.

The Government will also exempt temporary residents from Australian tax on most of their foreign source income for up to four years. This will provide tax relief of $105 million over 2007-08 and 2008-09, making it easier for Australian businesses to attract skilled workers to fill short-term vacancies, and help to ease cost pressures from employing foreign workers.

The Future Fund

With net debt dramatically reduced by this Government through continued surpluses and the use of asset sale proceeds to retire debt, the Government has made a further commitment to long-term fiscal sustainability by establishing a Future Fund to meet its unfunded superannuation liabilities, which currently amount to $91 billion.

The Future Fund will strengthen Australia's long-term financial position and ensure we are better able to meet the challenges of the future. Funding superannuation now will reduce future pressures on the budget at a time when the Government will need to face the spending challenges of an ageing population.

The Future Fund aims to accumulate sufficient financial assets to offset the Government's unfunded superannuation liabilities by 2020. The Government will commit accumulated surpluses of around $16 billion to the Fund as seed capital, once the 2004-05 Budget surplus is realised. These funds will be invested in a range of financial assets.

To ensure the Future Fund grows over time, the Government will reinvest its investment earnings in the Fund, which will be quarantined from the rest of the budget. The Government intends to invest future budget surpluses in the Fund. Legislation will be introduced to establish the Fund, which is to be managed by an independent statutory agency governed by an appropriately qualified board. The Government will set out an investment mandate to guide the board in managing the Fund. This legislation will prevent drawdowns from the Fund until the superannuation liability is considered by actuarial assessment to be fully funded. The Government will only be able to draw down the Fund to meet superannuation payments.

Supporting business in Australia

Providing tax and tariff relief for business

The Government will provide $1.8 billion in tax and tariff relief to business through a range of initiatives aimed at reducing cost pressures on business and supporting efficient and sustainable investment. The measures will help sustain high rates of productivity growth and increase the competitiveness of Australian business. Changes to international taxation arrangements will enhance Australia's attractiveness to foreign investors and as a location for regional headquarters, and will remove impediments to Australian firms investing overseas.

- The Government will remove the 3 per cent concessional tariff on business inputs that applies when there are no substitutable goods manufactured in Australia. The removal of the tariff will reduce business input costs by $1.25 billion over four years, helping to increase the international competitiveness of Australian business and encourage investment in efficient industries, so enhancing productivity.

- The Government will introduce a systematic treatment for 'blackhole' expenditures which will allow business to deduct a range of these expenses, including pre-business costs, which currently are not deductible for taxation purposes. 'Blackhole' expenditures are expenses which, currently, are not recognised under tax law. In addition, there will be increased scope for business to include expenditures in the cost base of an asset for capital gains tax purposes. The initiative will provide tax relief of $205 million over 2006-07 to 2008-09.

- The Government will make changes to align Australia's capital gains tax (CGT) regime for non-residents more closely with international norms, at a cost of $230 million over four years. These changes will narrow the operation of the CGT for non-residents by limiting its application to non-resident direct or indirect holdings of Australian real property (and similar assets, such as mining rights) and non-residents holding assets of a permanent establishment in Australia (branch assets). Bringing Australia into line with international practice will improve Australia's attractiveness as an investment destination.

- The foreign loss and foreign tax credit quarantining rules will be abolished. This will benefit Australian multinationals, regional headquarters operations in Australia, managed funds and small Australian businesses expanding offshore, at a cost of $50 million over 2007-08 to 2008-09. This budget also delivers the Government's election commitment to remove loss quarantining provisions that apply to film income.

- The Government will enhance the operation of the Petroleum Resource Rent Tax (PRRT) and the associated Gas Transfer Price Regulations to reduce industry compliance costs and improve administration. The changes will cost $23 million between 2006-07 and 2008-09, mainly due to changes to the timing of PRRT payments from allowing transferable exploration expenditure to be taken into account in calculating quarterly instalments of PRRT.

These measures build on previous tax initiatives for business, announced since the last budget, which provide targeted tax relief to small business, including the entrepreneur's tax offset (costing $1.2 billion over 2006-07 to 2008-09) and improved access to the simplified tax system (costing $361 million over four years).

This budget also provides a further $74 million to support small business through the continuation of the successful Small Business Assistance Programme, the Small Business Mentoring and Succession Programme, and the Business Entry Point website. The continuation of these programmes is recognition of the contribution the small business sector makes to the Australian economy and demonstrates the Government's commitment to supporting the entrepreneurial spirit of Australia's small businesses.

The Government will provide $12 million over four years to assist small businesses and their employees to form Australian Workplace Agreements, and provide a Workplace Dispute Settlement Pilot Programme to resolve disputes in a less formal and less costly way.

Investing in health and aged care

In 2005-06 the Government will spend $45 billion on health and aged care, up from $20 billion in the Government's first budget in 1996-97.

Targeting health priorities and investing in health promotion

This budget targets key health priorities and invests in health promotion, prevention and detection activities as part of a strategy to enhance the long-term health of Australians. Healthy individuals are more likely to enjoy opportunities to participate in the labour force and in society more generally, while minimising the growth of health costs.

This budget provides:

- $321 million over five years, including measures announced last year, to make dementia a National Health Priority and invest in early intervention, additional care services and carer training to significantly improve the quality of life for people with dementia;
- $208 million over five years to assist carers of senior Australians with more financial help and better access to respite care;
- $196 million over five years, including measures announced last year, through the Strengthening Cancer Care initiative to introduce coordinated measures that tackle prevention, treatment, research and support for cancer patients and their families and carers;
- $139 million over four years to fund new vaccines for chickenpox and polio, continuing the Government's strong commitment to child immunisation programmes;
- $79 million over four years to improve access to health services for veterans;
- $25 million over four years to implement a new National Tobacco Youth Campaign to help discourage young Australians from taking up smoking; and
- $22 million over four years in additional prevention, treatment and communication programmes as part of the National Illicit Drugs Strategy, which has received approximately $1 billion of Government funding since its introduction in 1997.

These initiatives build on the recently concluded Public Health Outcome Funding Agreements with the states and territories, which will provide $812 million funding over five years for public health initiatives, and on the Government's $116 million Building a Healthy, Active Australia package announced in 2004.

Creating a sustainable health system

However, Australia faces significant long-term pressures on health expenditure. Consistent with the requirements of responsible management, the Government is taking the necessary policy decisions to ensure the long-term viability of the health system. Failure to make changes today will put key government programmes at risk in the future.

The Government is raising the Medicare Safety Net thresholds to $500 for concession card holders and Family Tax Benefit Part A recipients and to $1000 for all other individuals and families. These threshold levels are those the Government originally proposed to the Senate. Setting the thresholds at these levels will save $499 million over four years, helping ensure the sustainability of this important government initiative.

The Medicare Safety Net will remain a generous protection against high medical expenses, with over $1.1 billion in benefits expected to be paid over the next four years. It also needs to be considered in the context of the Government's significant investment in Medicare, including the 100 per cent Medicare initiative, which has made GP services more affordable.

The Pharmaceutical Benefits Scheme (PBS) is the fastest growing component of health expenditure. The Government is committed to ensuring the sustainability of the PBS so all Australians can continue to have affordable access to necessary medicines, including through the listing of new innovative drugs as they become available.

In this budget, the Government is phasing in a moderate increase in the PBS Safety Net thresholds to further improve the balance of Government and consumer contributions. This measure builds on the 12.5 per cent mandatory price reduction for new generic drugs which will save an estimated $1 billion over five years.

The Government is pursuing needed reforms in the distribution and retailing of PBS medicines to contain the escalating costs. Through the next Community Pharmacy Agreement, the Government will ensure pharmacies are rewarded for the services they provide, without this placing an unfair burden on taxpayers. The Government will be seeking significant savings in this area in the next five-year Agreement, as well as substantial further savings over time.

A new approach to family law

The Government has a continuing strong commitment to Australian families.

This budget provides $398 million for reforms to the family law system focusing on families and their needs before, during and after separation. Increased services will help prevent separation and, where parents do separate, will allow a less adversarial path to separation through:

- A network of 65 community-based Family Relationship Centres at a cost of $199 million over four years. These will underpin a fresh approach to the family law system, putting the emphasis on reaching agreement on child custody arrangements at a much earlier stage in the separation process, outside and before formal court proceedings. As part of this initiative, $10 million will be provided to Rural Outreach Services;

- $137 million over four years to maintain the increased funding to family relationship services provided in 2004-05 and for a significant expansion of pre-marriage education, early intervention services for families and Men’s Line; and

- $54 million over four years to expand the successful Contact Orders Programme, children's contact services, dispute resolution counselling, mediation and similar services.

Assistance for Indigenous Australians

This budget provides substantial extra assistance for Indigenous Australians.

- $86 million will be provided over four years to continue to develop and implement Shared Responsibility Agreements. A key priority in this process will be further fostering community engagement in goal setting and decision making processes.

- In employment and business development, the Community Development Employment Projects (CDEP) programme will be reformed to give more outcome-focused funding agreements, and an Indigenous Economic Development Strategy will be implemented to identify and foster entrepreneurs.

- In health, the Government will provide $102 million over four years to improve the health of Indigenous babies and children, through targeted activities in maternal and child health and chronic disease. An additional $40 million will be provided to the Primary Health Care Access Programme to further improve access to health services by establishing new primary health sites and increasing the capacity of existing clinics. Some $10 million will increase access to hearing services for Indigenous adults, and $18 million will help to address substance misuse.

- In housing, the Government will invest $103 million over four years to continue and expand the Healthy Indigenous Housing initiative to meet, more efficiently and effectively, the housing needs of Indigenous communities.

Providing for Australia’s Security

National security remains a priority for the Government.

The Government continues to increase resources for Australia’s security agencies to meet the higher demands placed on them. As part of its integrated national security strategy, the Government supports cooperation between national and international agencies, and links to business and the community.

In each budget since 11 September 2001, the Government has invested significantly to improve national security. In total, it has committed $5.6 billion over eight years from 2001-02 to foster safety and security in Australia and our region.

This budget provides $1.1 billion over four years for protective security enhancements, border security, intelligence, regional security initiatives and incident response capacity. The *Providing for Australia's Security* package includes:

- $522 million for protective security enhancements, including for Defence personnel and facilities and Australia's overseas missions, such as enhanced emergency communications and relocation of some missions;
- $226 million for border protection, including a significant investment in new biometric technologies, incorporating ePassports, to help border authorities to verify travellers' identities quickly and reliably;
- $239 million to strengthen Australia's intelligence capabilities, including for counter-terrorism investigations and language skills development;
- $60 million for regional security initiatives, including cooperation and knowledge sharing and counter-terrorism assistance measures; and
- $26 million to build Australia's incident response capability, including resources for counter-terrorism prosecutions.

Enhancing quarantine and protecting Southern Ocean fisheries

The Government is committed to maintaining the integrity of Australia's borders.

Australia's quarantine regime provides a strong forward defence against exotic diseases, protecting Australia's unique biodiversity and maintaining the market advantage associated with the Australian agriculture sector's 'clean and green' image. In this budget, the Government commits $580 million over four years to maintain and enhance our quarantine inspection regime. This includes:

- $391 million for maintaining Australia's commitment to manage quarantine risk and protect our borders;
- $144 million for continuing the Government's 40 per cent contribution to quarantine inspection fees and charges, to help Australian agricultural exports to be more price competitive in overseas markets;
- $39 million for enabling Biosecurity Australia to conduct import risk assessments and promote Australia's quarantine system internationally; and
- $6 million for enhancing border controls at Australia's airports in response to the increased risk of avian influenza to both humans and animals in our region.

This budget also provides $181 million over four years from 2006-07 to continue armed patrols of Australia's exclusive economic zone in the Southern Ocean. These patrols aim to suppress the activities of vessels engaged in illegal fishing, as well as protect Australia's sovereign interests in, and the environmental values of, the Southern Ocean.

International engagement

The future wellbeing of Australians depends on our ability to gain from trade and other links with the rest of the world, while limiting exposure to external risks. Australia has a clear interest in promoting sustainable development in our region and globally. The Government is pursuing an active, practical and multilayered strategy to meet these challenges. Key instruments include providing bilateral assistance and actively participating in global and regional institutions and forums.

Providing bilateral assistance

The Government has committed $1 billion over five years to help Indonesia recover from the devastating human and economic damage caused by the Boxing Day tsunami. These funds will be divided equally between grant assistance and highly concessional loans. Combined with Australia’s existing development cooperation programme, this brings Australia’s commitment to Indonesia to a total of $1.8 billion over five years.

The Government will provide funding of $69 million over the next four years to develop a tsunami warning system which will provide 24 hour surveillance for accurate and early detection and warning in the event of a tsunami threatening the west or east coast of Australia, or South West Pacific nations.

This budget continues funding to the Regional Assistance Mission to the Solomon Islands at a cost of $841 million over four years. The Government will also continue its substantial commitments of personnel to strengthen capacity in Papua New Guinea and, on a smaller scale, Nauru.

Australia has a strong interest in a stable and developing Iraq. This budget provides $466 million over four years to continue the Australian Defence Force’s contribution to stabilisation and reconstruction activities. This includes $240 million over four years for Defence deployments in the Al Muthanna Province in southern Iraq, and $226 million over three years to continue Operation CATALYST. Additional funding of $45 million over two years will assist Iraq’s economic development and democratic transition.

The Government is maintaining its strong support for the World Bank’s Heavily Indebted Poor Countries (HIPC) Initiative, which aims to reduce the excessive debt burdens of the world’s poorest nations. This budget provides an additional $35 million over three years to the HIPC Initiative. The effect of Australia’s increased aid commitments will be to raise official development assistance (ODA) by $518 million from 2003-04 to 2005-06. This will increase the ratio of ODA to gross national income from 0.25 in 2003-04 to 0.28 in 2005-06.

PART 2
FISCAL AND ECONOMIC OUTLOOK

This part presents the main budget aggregates for the 2005-06 Budget and reconciles these with estimates from the 2004-05 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 discusses the outlook for the domestic and international economies.

This part also discusses the Australian economy's recent strong performance and the scope to sustain our prosperity. Policies and choices that support rapid productivity growth and widespread participation in the economy and society can further the wellbeing of all Australians.

STATEMENT 2: FISCAL OUTLOOK

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

The fiscal outlook for Australia remains strong, with the Government forecasting an underlying cash surplus of $8.9 billion in 2005-06. Across the forward estimates, the Government has maintained the budget in a strong surplus position after providing for personal income tax cuts of $21.7 billion and a $3.6 billion welfare reform package.

The Government's sound fiscal management will see further reductions to net debt across the forward years. The continued strengthening of net worth through strong surpluses and initiatives such as the Future Fund leaves government finances well placed to deal with the medium-term fiscal pressures projected in the Productivity Commission's recent report on the *Economic Implications of an Ageing Australia*.

This Budget provides for around $16 billion to be allocated to the Future Fund in 2005-06.

STATEMENT 2: FISCAL OUTLOOK

The fiscal outlook for Australia remains strong, with the Government forecasting its eighth budget surplus. Across the forward estimates period, the Government has maintained the budget in surplus after providing $21.7 billion of personal income tax cuts, $3.6 billion on a *Welfare to Work* package to improve work incentives and labour force participation and $2.5 billion to abolish the superannuation surcharge.

BUDGET AGGREGATES

An underlying cash surplus of $8.9 billion is expected in 2005-06 compared with an estimated surplus of $4.5 billion at the *Mid-Year Economic and Fiscal Outlook 2004-05* (MYEFO). Underlying cash surpluses are projected to continue across the forward estimates.

In accrual terms, a fiscal surplus in 2005-06 of $7.4 billion is forecast compared to $3.5 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		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
Revenue ($b)	**187.6**	**202.7**	**214.5**	**222.9**	**233.4**	**245.3**
Per cent of GDP	23.1	23.5	23.1	23.0	23.2	23.1
Expenses ($b)	**182.0**	**195.0**	**206.1**	**214.8**	**225.4**	**236.6**
Per cent of GDP	22.4	22.6	22.2	22.2	22.4	22.3
Net operating balance ($b)	5.6	7.7	8.4	8.1	8.0	8.8
Net capital investment ($b)	0.7	0.7	1.0	0.6	0.0	-0.3
Fiscal balance ($b)	**4.8**	**7.0**	**7.4**	**7.5**	**8.0**	**9.0**
Per cent of GDP	0.6	0.8	0.8	0.8	0.8	0.9
Underlying cash balance ($b)(b)	**8.0**	**9.2**	**8.9**	**7.9**	**8.5**	**9.3**
Per cent of GDP	1.0	1.1	1.0	0.8	0.8	0.9
Memorandum item:						
Headline cash balance ($b)	7.6	7.9	7.9	18.2	18.6	19.4

(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.
(b) Excludes expected Future Fund earnings from 2005-06 onwards. For further explanation refer to Statement 2 Box 1 and Statement 8.

VARIATIONS TO THE FISCAL BALANCE ESTIMATES

The upward revision of $3.9 billion in the 2005-06 fiscal surplus since MYEFO largely reflects higher than anticipated revenue from companies, small unincorporated businesses and personal investors. This is partly offset by the impact of personal income tax cuts and the Government's *Welfare to Work* package.

Table 2 provides a reconciliation of the fiscal balance estimates between the 2004-05 Budget, the 2004-05 MYEFO and the 2005-06 Budget.

Table 2: Reconciliation of 2004-05 Budget, 2004-05 MYEFO and 2005-06 Budget fiscal balance estimates

	Estimates		Projections	
	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m
2004-05 Budget fiscal balance	**698**	**712**	**2,291**	**2,619**
Per cent of GDP	0.1	0.1	0.2	0.3
Changes between 2004-05 Budget and MYEFO				
Effect of policy decisions(a)				
Revenue	-11	-401	-1,115	-1,025
Expenses	1,646	2,943	3,250	3,367
Net capital investment	227	116	104	172
Total policy decisions impact on fiscal balance(b)	-1,885	-3,460	-4,469	-4,564
Effect of parameter and other variations				
Revenue	6,303	6,514	6,486	7,237
Expenses	-142	16	-919	-1,418
Net capital investment	330	254	244	133
Total parameter and other variations impact on fiscal balance(b)	6,115	6,245	7,161	8,522
2004-05 MYEFO fiscal balance	**4,929**	**3,497**	**4,984**	**6,577**
Per cent of GDP	0.6	0.4	0.5	0.6
Changes between MYEFO and 2005-06 Budget				
Effect of policy decisions(a)				
Revenue	-35	-3,472	-6,675	-7,662
Expenses	932	2,040	3,041	3,201
Net capital investment	12	251	166	83
Total policy decisions impact on fiscal balance(b)	-978	-5,763	-9,882	-10,946
Effect of parameter and other variations				
Revenue	3,258	10,486	11,986	11,725
Expenses	272	456	-598	-690
Net capital investment	-66	354	228	44
Total parameter and other variations impact on fiscal balance(b)	3,053	9,676	12,356	12,372
2005-06 Budget fiscal balance	**7,003**	**7,410**	**7,458**	**8,003**
Per cent of GDP	0.8	0.8	0.8	0.8

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

Variations in revenue estimates

Total revenue for 2005-06 has been revised up by $7.0 billion since MYEFO, reflecting higher estimated revenue from companies, personal investors and small unincorporated businesses. These upward revisions have been partly offset by the impact of the Government's decision to provide further personal income tax cuts.

Policy decisions since the 2004-05 MYEFO are expected to reduce taxation revenue by around $3.5 billion in 2005-06 and around $26.1 billion over the forward years. The major policy decisions affecting revenue over the four year period 2005-06 to 2008-09 are outlined below.

- The personal income tax cuts taking effect from 1 July 2005 and 1 July 2006 will reduce revenue by $3.1 billion in 2005-06, and $21.7 billion over the forward estimates period.

- The abolition of the superannuation contributions and termination payments surcharge for contributions made from 1 July 2005 will reduce revenue by $650 million in 2006-07 and $2.5 billion over the forward estimates.

- The removal of the 3 per cent tariff applying to business inputs imported under a tariff concession order, effective from 11 May 2005, will reduce revenue by $36 million in 2004-05, $290 million in 2005-06 and $1.3 billion over the forward estimates.

- The extension of the eligibility criteria for the mature age worker tax offset will reduce revenue by $70 million in 2005-06 and $295 million over the forward estimates period.

- A four-year income tax exemption for temporary residents for most foreign source income, including capital gains, commencing from July 2006, will reduce revenue by $50 million in 2007-08 and $105 million over the forward estimates.

- Changes to the capital gains tax treatment of non-resident investors in Australia will reduce revenue by $50 million in 2005-06 and $230 million over the forward estimates.

- Recognition for tax purposes of certain currently unrecognised business capital expenditures ('blackhole expenditures') from 2006-07 will reduce revenue by $35 million in 2006-07, increasing in later years, to a cost of $205 million over the forward estimates.

- Changes to the capital allowance treatment of film copyright to ensure the application of the effective life depreciation regime, with effect to expenditures after 1 July 2004, will reduce revenue by $15 million in 2005-06 and $175 million over the forward estimates.

- Abolition of the foreign loss and foreign tax credit quarantining, with effect from the first income year after Royal Assent, will reduce revenue by $25 million in 2007-08 and in 2008-09.

Parameter and other variations are expected to increase revenue in 2005-06 by $10.5 billion, relative to the MYEFO forecasts. These upward revisions reflect the flow on effect of a stronger expected revenue base in 2004-05 and a significant upward revision to nominal GDP growth in 2005-06.

- Relative to MYEFO, nominal GDP growth for 2005-06 has been revised up by 1¾ percentage points to 7½ per cent — despite a slight downward revision to real GDP growth — reflecting significant increases in estimated growth in the GDP deflator as a result of recent increases in commodity export prices (see Box 3, Statement 3).

- These increases are expected to lift corporate profits significantly in 2005-06, which — due to the timing of company tax collections — will boost revenue in both 2005-06 and 2006-07. Reflecting this, estimated company income tax revenue for 2005-06 has been revised up by $4.7 billion since MYEFO, and by a further $3.8 billion in 2006-07.

The Budget estimates also incorporate adjustments to forecasting methodology to align the estimates more closely with recent experience (see Box 1, Statement 5). These adjustments affect the gross other individuals, refunds for individuals and company income tax revenue heads and generally increase estimated revenue from MYEFO for 2005-06 and the projection years.

Relative to MYEFO, estimated total revenue for 2004-05 has been revised up by $3.2 billion, largely owing to higher expected revenue from wage and salary earners, personal investors and small unincorporated businesses.

More detail on how the revised outlook for the economy has affected individual revenue heads over the forward estimates period is provided in Statement 5. A full description of all policy measures since MYEFO is provided in Budget Paper No. 2, *Budget Measures 2005-06*.

Variations in expense estimates

Since MYEFO, estimated expenses for 2005-06 have increased by $2.5 billion reflecting the impact of new policy decisions of $2.0 billion and parameter and other variations of $0.5 billion.

Major policy decisions since MYEFO that have increased expenses include:

- $430 million in 2005-06 ($2 billion over the five years from 2004-05) to increase the maximum rate of Family Tax Benefit Part B, as announced in the *Extra Assistance for Families* election commitment;

- $207 million in 2005-06 ($797 million over four years) to continue assisting the Solomon Islands Government in the restoration of law and order and broad-ranging economic, governance and public sector reforms;

- $177 million in 2005-06 ($211 million over four years from 2004-05) for the deployment of additional troops to provide security and training in Southern Iraq;

- $174 million in 2005-06 ($211 million over three years from 2004-05) to continue the Australian Defence Force contribution to stabilisation and reconstruction activities in Iraq (Operation Catalyst);

- $170 million in 2005-06 ($3.5 billion over four years) for the *Welfare to Work* package to increase workforce participation and reduce welfare dependency while retaining a strong safety net for those in need;

- $115 million in 2005-06 ($500 million over five years from 2004-05) for the grants component of the Australian-Indonesia Partnership for Reconstruction and Development Package to help Indonesia restore health, education and local government services in the worst tsunami affected areas, and improve economic governance and public administration. This is in addition to the $500 million in concessional loans over five years to be directed to reconstruction and rehabilitation of major infrastructure across Indonesia; and

- $112 million in 2005-06 ($579 million over four years) to continue funding for quarantine border protection programmes delivered by the Australian Quarantine and Inspection Service, the Australian Customs Service and Biosecurity Australia.

Major policy decisions reducing expenses include:

- a $139 million reduction in 2005-06 ($1 billion over five years from 2004-05) due to changes to listing arrangements for pharmaceuticals which will see a price reduction of at least 12.5 per cent when the first new brand of an already listed medicine is added to the Pharmaceutical Benefits Scheme; and

- an $84 million decrease in 2005-06 ($335 million over four years) resulting from the withdrawal of the funding offer to state and territory governments to extend concessions to Commonwealth Seniors Health Card holders.

In 2005-06, parameter and other variations have increased forecast expenses by $0.5 billion since MYEFO largely reflecting:

- a $588 million increase in estimated civilian superannuation expenses, largely due to higher nominal interest expense reflecting changes in the estimate of the Consumer Price Index;

- a $398 million increase in Defence expenses reflecting an increase in the estimated non-farm GDP deflator, which is used to index Defence operating expenses;
- a rephasing of $300 million by the Department of Defence of its major capital equipment acquisition programme from beyond the forward estimates period into 2005-06 to meet current funding requirements, including from expected improvements in performance in the delivery of the Defence Capability Plan;
- a $232 million increase in expenses administered by the Australian Taxation Office resulting from a change in accounting policy which recognises certain payments in the year of accrual rather than the year of payment;
- a $220 million increase in expenses due to a reclassification of Defence Housing Authority expenses following the adoption of the Inventory Accounting Standard which has resulted in expenses being recognised for the purpose of Government Finance Statistics;
- a $200 million increase in Energy Grants Credit Scheme expenses, flowing on from higher than forecast claims activity in 2004-05 due to expected increases in the mining and road transport sectors; and
- a $70 million increase in Private Health Insurance Rebate expenses, primarily resulting from higher than expected premium increases and levels of insurance coverage.

The above increase in expenses is partially offset by:

- a $439 million reduction in anticipated Newstart Allowance and Youth Allowance expenses, largely due to the stronger labour market reducing the expected number of unemployment benefit recipients;
- a $120 million reduction for Superannuation Guarantee Programme expenses, primarily due to delays in processing claims;
- a $69 million reduction in expenses for the Cleaner Fuels Grant Scheme due to a lower than forecast take-up of bio-diesel production grants;
- the removal of the provision for the implementation of election commitments now reported as policy measures; and

- the regular draw-down of the conservative bias allowance[1] reducing estimated expenses by around $1 billion each year from 2005-06.

In 2004-05, estimated expenses have increased by $1.2 billion since MYEFO. This largely reflects new spending of $932 million including $314 million for a one-off lump-sum payment to eligible carers and $212 million towards the Family Tax Benefit Part B package. Parameter and other variations have increased expenses by $272 million and include a $1 billion increase in expenses administered by the Australian Taxation Office resulting from a change in accounting policy, partially offset by other variations including a $140 million underspend associated with the delayed deployment of Australian Federal Police staff to Papua New Guinea.

More detailed information on expenses can be found in Statement 6. A full description of all policy measures since MYEFO can be found in Budget Paper No. 2, *Budget Measures 2005-06*.

Variations in net capital investment estimates

In 2005-06, forecast net capital investment has increased by $605 million since the 2004-05 MYEFO. This represents the combined effect of:

- new policy measures of $251 million, including $56 million largely to ensure the *Welfare to Work* reforms are supported by high quality information technology, $42 million of additional investment in improved security for Australian diplomatic missions, $16 million to continue assisting the Solomon Islands Government in the restoration of law and order and broad ranging economic, governance and public sector reforms, and $11 million for the deployment of additional troops to provide security and training in Southern Iraq; and

- parameter and other variations of $354 million, largely due to a $195 million revision in estimated Defence Housing Authority sales, $101 million in capital investment by the Overseas Property Office and a further $34 million investment for the construction of the Christmas Island Immigration Reception and Processing Centre. These increases are partially offset by sales in the Defence Property Sales programme estimated at $89 million.

In 2004-05, estimated net capital investment has decreased by $54 million since MYEFO, largely reflecting parameter and other variations.

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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. To offset this the contingency reserve includes an allowance based on past experience to preserve the overall integrity of forward estimates. This allowance, known as the conservative bias allowance, is progressively reduced so that the budget year conservative bias allowance is zero by budget night.

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 2005-06*.

CASH FLOWS

In 2005-06, an underlying cash surplus of $8.9 billion is expected, compared with the MYEFO estimate of $4.5 billion. The improvement in the underlying cash surplus is largely due to the same variations that affect the fiscal balance. From 2005-06 onwards, the exclusion of Future Fund earnings lowers the underlying cash balance relative to the fiscal balance.

Box 1: Budget treatment of expected Future Fund earnings

The Government has announced that it will establish a Future Fund to offset superannuation liabilities that would otherwise be a burden to future generations.

The Government is reporting the underlying cash balance excluding Future Fund earnings from 2005-06 onwards because the earnings will be reinvested to meet future superannuation payments and are therefore not available for current spending. However, Future Fund earnings are included in the fiscal balance because superannuation expenses relating to future cash payments are recorded in the fiscal balance estimates.

The rate of return on the Future Fund investments will depend on the actual asset allocation across different asset classes. Once the enabling legislation has passed, the Future Fund Management Board will be responsible for investments in accordance with a broad investment mandate. In the absence of an investment mandate, the budget and forward estimates assume the initial investment of seed capital will earn a return equal to yields on other term deposits held by the Government.

Expected Future Fund earnings are separately identified in the Australian Government cash flow statement in Statement 2, Appendix B and the historic tables in Statement 13.

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		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$b	$b	$b	$b	$b
Cash receipts					
Operating cash receipts	202.2	214.2	221.7	232.3	244.1
Capital cash receipts(b)	0.4	0.3	0.2	0.3	0.2
Total cash receipts	202.7	214.5	221.9	232.5	244.2
Cash payments					
Operating cash payments	190.9	202.0	210.4	220.7	231.9
Capital cash payments(c)	2.6	3.1	2.5	2.3	2.0
Total cash payments	193.4	205.1	213.0	223.0	233.9
Finance leases and similar arrangements(d)	0.0	0.0	0.0	0.0	0.0
GFS cash surplus(+)/deficit(-)	9.2	9.4	8.9	9.5	10.3
Per cent of GDP	1.1	1.0	0.9	0.9	1.0
less Future Fund earnings	0.0	0.5	0.9	1.0	1.1
Underlying cash balance(e)	**9.2**	**8.9**	**7.9**	**8.5**	**9.3**
Per cent of GDP	1.1	1.0	0.8	0.8	0.9
Memorandum items:					
Net cash flows from investments in financial assets for policy purposes(f)	-1.3	-1.5	9.3	9.1	9.0
plus Future Fund earnings	0.0	0.5	0.9	1.0	1.1
Headline cash balance	**7.9**	**7.9**	**18.2**	**18.6**	**19.4**

(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) Excludes expected Future Fund earnings from 2005-06 onwards. For further explanation refer to Statement 2 Box 1 and Statement 8.
(f) 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

	Estimates		Projections	
	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m
2004-05 Budget underlying cash balance	**2,391**	**1,587**	**3,438**	**4,501**
Changes from 2004-05 Budget to MYEFO				
Effect of policy decisions(a)	-1,728	-3,355	-4,423	-4,541
Effect of parameter and other variations	5,543	6,227	6,682	7,625
Total variations	**3,816**	**2,872**	**2,259**	**3,084**
2004-05 MYEFO underlying cash balance	**6,206**	**4,459**	**5,697**	**7,584**
Changes from MYEFO to 2005-06 Budget				
Effect of policy decisions(a)	-744	-5,755	-9,377	-10,687
Effect of parameter and other variations	3,759	10,678	12,556	12,600
Total variations	**3,015**	**4,923**	**3,179**	**1,912**
less Future Fund earnings	0	462	943	997
2005-06 Budget underlying cash balance(b)	**9,221**	**8,921**	**7,933**	**8,500**

(a) Excludes the public debt net interest effect of policy measures.
(b) Excludes expected Future Fund earnings from 2005-06 onwards. For further explanation refer to Statement 2 Box 1 and Statement 8.

While the 2005-06 fiscal balance has increased by $3.9 billion since MYEFO, the underlying cash balance has increased by $4.5 billion. This difference between the change in the underlying cash balance and the fiscal balance largely reflects increased superannuation expenses and Australian Taxation Office administered expenses resulting from a change in accounting treatment which affect the fiscal balance but not the cash balance. These differences are partly offset by Future Fund earnings, which are included in the fiscal balance but excluded from the underlying cash balance.

Headline cash balance

A headline cash surplus of $7.9 billion is now forecast for 2005-06 compared with a surplus of $3.0 billion at MYEFO. The increase in the headline cash surplus estimate since MYEFO largely reflects the increase in the underlying cash balance plus the inclusion of expected Future Fund earnings.

NET DEBT AND NET WORTH

With the budget remaining in cash surplus in 2005-06 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 fall to $6.1 billion (0.7 per cent of GDP) by the end of 2005-06. Net interest payments are also expected to fall over the forward estimates.

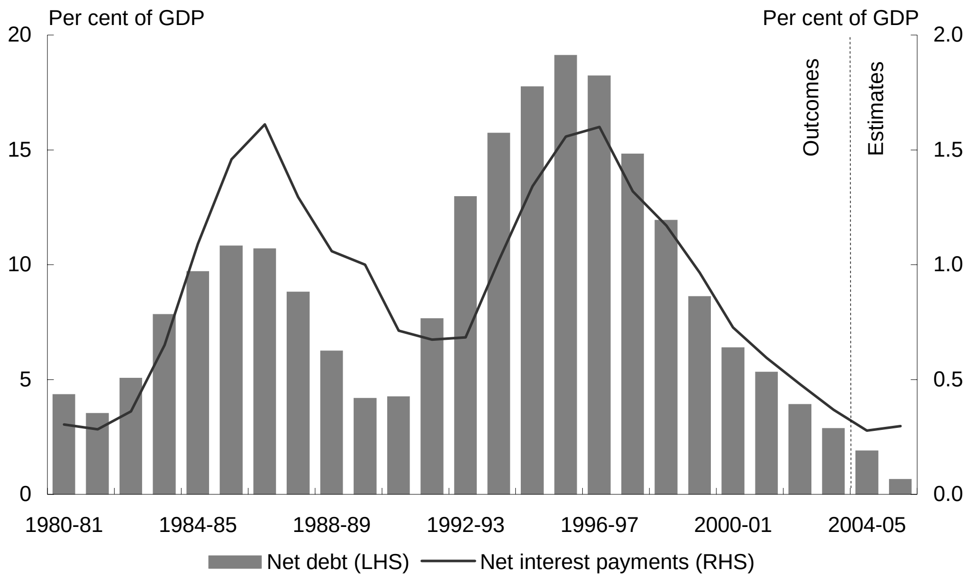
Table 5 and Chart 1 provide a summary of Australian Government general government sector net worth, net debt and net interest payments.

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

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$b	$b	$b	$b	$b
Financial assets	119.4	127.9	138.5	151.5	163.4
Non-financial assets	41.3	42.4	43.1	43.0	42.8
Total assets	**160.6**	**170.3**	**181.6**	**194.5**	**206.2**
Total liabilities	**194.7**	**198.1**	**202.0**	**208.2**	**212.1**
Net worth	**-34.1**	**-27.8**	**-20.4**	**-13.7**	**-5.9**
Net debt(a)(b)	**16.3**	**6.1**	**-14.0**	**-34.6**	**-56.4**
Per cent of GDP	1.9	0.7	-1.5	-3.4	-5.3
Net interest payments(c)	**2.4**	**2.8**	**1.2**	**-0.2**	**-1.3**
Per cent of GDP	0.3	0.3	0.1	0.0	-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 shareholding in Telstra, but may change as a result of the establishment of the Future Fund.
(c) Australian Government cash interest payments less cash interest receipts. The 2005-06 estimates 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 net debt projections have improved considerably since MYEFO, reflecting larger than anticipated cash surpluses.

Australia's net debt position compares favourably to other industrialised countries. 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).

Having peaked at $8.4 billion in 1996-97, net interest payments are expected to decline to $2.8 billion in 2005-06, representing annual interest savings of around $5.7 billion.

Net worth is expected to improve from -$34.1 billion in 2004-05 to -$5.9 billion in 2008-09, mainly reflecting cumulative surpluses in the forward estimates. The prospects for net worth mean the Government's finances are well placed to deal with emerging fiscal pressures.

MEDIUM-TERM FISCAL OUTLOOK

Importance of fiscal sustainability

Delivering sustainable fiscal policy is a key requirement of good government. By not living beyond its means, the Government prevents costly burdens being placed on future generations. Further, when governments are fiscally responsible, they provide a secure investment environment that encourages growth.

By reducing debt to manageable levels, the Government has put its finances in a sound position and generated substantial savings that can be directed to other purposes. However, sustainable fiscal policy is more than just prudent reduction of past debts. It involves managing all elements of the balance sheet — such as the unfunded superannuation liability — and a forward-looking strategy to address the looming fiscal pressures yet to affect Government finances.

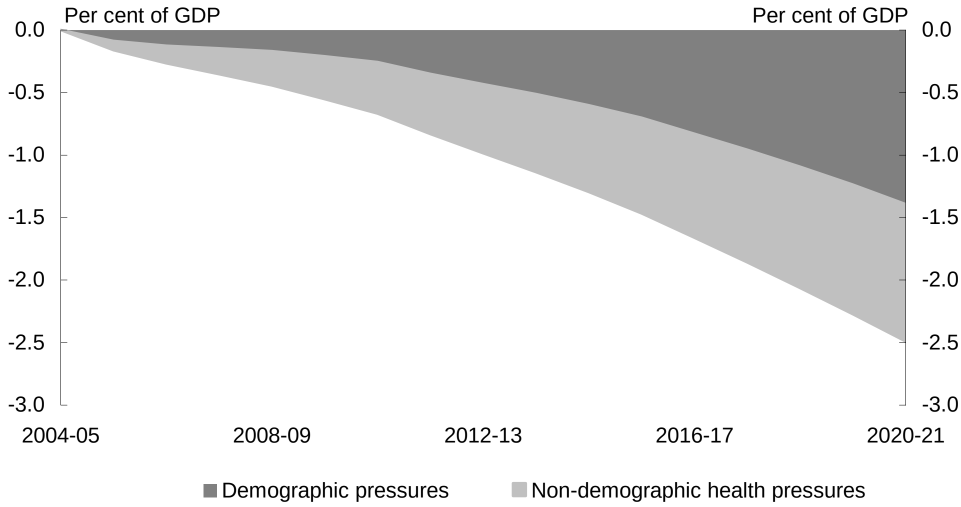
The Government recognised the importance of fiscal sustainability by committing to the regular release of the Intergenerational Report, with the first report in 2002 foreshadowing a significant fiscal gap opening over the long term. The Government is committed to managing these fiscal pressures by implementing pro-growth policies that raise productivity and encourage greater participation in the economy. The Government complements this by taking a long-term view when managing the fiscal outlook. Without making moderate reforms today, more drastic policy solutions will become inevitable in the future.

Medium-term budget pressures

While the current budget position is strong, significant fiscal pressures will emerge beyond the forward estimates period. Demographic change is expected to lead to both lower taxation receipts — due to falls in workforce participation — and higher payments, mainly for pensions and health care. In this budget, the GDP projection in 2008-09 has been lowered by ¼ per cent, reflecting the initial step of recognising slowing economic growth from the ageing of the population. Medium-term pressures are generated from rising health care costs, relating to increasing demand for health services, technological advances and demographic change.

While these fiscal pressures are most evident over the long term, they will have significant effects within the next ten years. The Productivity Commission's report on the *Economic Implications of an Ageing Australia* suggests that a fiscal gap of around 1.5 per cent of GDP will emerge by 2015-16; equivalent to $13 billion in today's terms. A breakdown of the impact of these fiscal pressures is reflected in Chart 1 below.

Chart 1: Medium-term fiscal pressures



Source: Productivity Commission, 2005, *Economic Implications of an Ageing Australia.*

Improving fiscal sustainability

The Government already has a strong record on fiscal sustainability by reducing net debt by an estimated $90 billion, from 19 per cent of GDP in 1995-96 to 0.7 per cent of GDP in 2005-06. This has freed up interest savings of around $5.7 billion annually that can be applied to other fiscal pressures. In addition, the Government has released a series of packages designed to lower fiscal pressures over the medium to long term.

The Government's currently unfunded superannuation liability to employees is the largest liability on the balance sheet at around $91 billion in 2004-05. By establishing the Future Fund, the Government has pre-committed resources to meet future superannuation payments. As Future Fund earnings are not available for other spending, they are excluded from the underlying cash balance. Funding superannuation now will reduce future pressures on the budget at a time when the Government will need to face the spending challenges of an ageing population.

In addition to establishing the Future Fund, the Government has closed entry to the Public Sector Superannuation Scheme to limit future growth in the liability. Overall, these reforms ensure that superannuation costs are not passed onto future generations at a time when other demographic pressures emerge.

Also in this budget the Government has announced a comprehensive reform package that will improve the outlook for workforce participation and place the welfare system on a more sustainable basis. New obligations to seek part-time work will ensure that those who are able to work do so. The combination of improved payment and income test arrangements, a new compliance regime that encourages people to meet their obligations and funding for a range of new and expanded services will increase participation by moving people out of welfare and into work.

Also, the introduction of the Child Care Tax Rebate and the provision of additional child care places assist parents returning to the workforce after having children. Together, these packages will lead to greater workforce participation that strengthens both the overall economy and the Government's finances over the medium term.

Healthcare costs currently represent 18 per cent of the Government expenses and will continue to grow strongly in the future. In particular, expenses for the Pharmaceutical Benefits Scheme increased by 11 per cent in 2003-04, reflecting higher general demand for health services — an effect that will be compounded through demographic change. The increase in PBS patient co-payments, the mandatory 12.5 per cent price reduction for generic drugs as well as the raising of the Medicare Safety Net thresholds are directed to returning healthcare to a sustainable footing so that future generations can also enjoy high quality health services.

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 for budget reporting purposes are:

- the Australian Bureau of Statistics' (ABS) accrual Government Finance Statistics (GFS) publication *Australian System of Government Finance Statistics: Concepts, Sources and Methods* Cat. No. 5514.0, which in turn is based on the International Monetary Fund (IMF) accrual GFS framework; and
- Australian Accounting Standards (AAS), including AAS 31 *Financial Reporting by Governments*.

The operating statement and balance sheet include an adjustment to take account of the estimated impact of the Australian Equivalents to International Financial Reporting Standards (AEIFRS) on Australian Government general government sector reporting. There is no immediate direct impact on the underlying cash balance and the GFS surplus/deficit in this statement and in Statement 9. There is an impact on both the fiscal balance and net worth in this statement and in the general government sector of Statement 9. The AEIFRS reporting requirements and impact on the AAS Statement of Financial Performance and Statement of Financial Position are outlined in Note 2 of Statement 10.

The 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. However, 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.

ABS GFS 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 AAS financial statements currently record IMF Special Drawing Rights (SDRs) as a liability. This is consistent with AAS. The GFS statements also record SDRs as a liability. However, in accordance with the IMF"s GFS manual, IMF SDRs are not treated as a liability in ABS GFS 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 IMF, and developments in train to harmonise GFS and AAS.

Similarly, the GFS financial statements currently adopt the AAS 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 ABS GFS, coins on issue are treated as a liability and no revenue is recognised. The current accounting treatment will remain in place pending further consultation with the IMF, and developments in train to harmonise GFS and AAS.

The ABS GFS 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 and measured. This treatment does not affect the underlying cash or fiscal balances.

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. This method is permitted under both GFS and AAS when there is an inability to reliably measure taxation revenue at the time the underlying transactions or events occur. 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

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Revenue					
Taxation revenue	190,201	201,267	208,999	218,798	230,120
Current grants and subsidies	0	0	0	0	0
Sales of goods and services	4,828	4,965	5,194	5,330	5,363
Interest income	1,562	2,000	2,853	3,997	5,025
Dividend income	3,146	3,312	2,952	2,357	1,852
Other	2,929	2,967	2,884	2,924	2,966
Total revenue	**202,666**	**214,511**	**222,882**	**233,405**	**245,326**
Expenses					
Gross operating expenses					
Depreciation	1,892	2,140	2,252	2,341	2,361
Superannuation	2,487	2,363	2,409	2,434	2,479
Salaries and wages	11,922	12,617	12,828	13,164	13,668
Payment for supply of goods and services	45,246	48,395	50,538	52,858	54,020
Other operating expenses	2,814	2,584	2,618	2,770	2,917
Total gross operating expenses	*64,362*	*68,100*	*70,645*	*73,567*	*75,444*
Nominal superannuation interest expense	4,882	5,713	5,594	5,821	5,947
Other interest expenses	4,131	3,851	3,774	3,761	3,574
Other property expenses	0	0	0	0	0
Current transfers					
Grant expenses	37,203	40,559	40,742	42,293	42,892
Subsidy expenses	6,470	6,560	6,697	6,936	7,466
Personal benefit payments in cash	74,478	77,545	83,258	88,742	97,033
Other current transfers	0	0	0	0	0
Total current transfers	*118,151*	*124,664*	*130,697*	*137,972*	*147,390*
Capital transfers	3,486	3,754	4,097	4,279	4,213
Total expenses	**195,012**	**206,081**	**214,806**	**225,400**	**236,568**
Net operating balance	**7,655**	**8,430**	**8,076**	**8,005**	**8,758**
Net acquisition of non-financial assets					
Purchases of non-financial assets	2,487	2,920	2,392	2,429	2,104
less Sales of non-financial assets	364	285	174	250	188
less Depreciation	1,892	2,140	2,252	2,341	2,361
plus Change in inventories	374	340	473	273	270
plus Other movements in non-financial assets	47	185	178	-111	-89
Total net acquisition of non-financial assets	**652**	**1,020**	**617**	**1**	**-264**
Net lending/fiscal balance(a)	**7,003**	**7,410**	**7,458**	**8,003**	**9,022**

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

Table B2: Australian Government general government sector balance sheet

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Assets					
Financial assets					
Cash and deposits	927	288	459	210	143
Advances paid	19,314	20,536	22,001	23,921	26,059
Investments, loans and placements(a)	31,066	38,096	56,389	77,150	96,186
Other non-equity assets	17,147	17,856	19,477	21,336	23,410
Equity(b)	50,895	51,137	40,166	28,854	17,570
Total financial assets	*119,351*	*127,913*	*138,493*	*151,472*	*163,368*
Non-financial assets					
Land	4,863	5,161	5,119	5,027	4,973
Buildings	13,894	14,008	14,263	14,428	14,536
Plant, equipment and infrastructure	8,411	8,578	8,716	8,546	8,256
Inventories	5,299	5,570	5,989	6,228	6,463
Heritage and cultural assets	6,698	6,739	6,766	6,787	6,808
Other non-financial assets	2,085	2,341	2,207	2,006	1,762
Total non-financial assets	*41,250*	*42,397*	*43,060*	*43,022*	*42,798*
Total assets	**160,601**	**170,310**	**181,553**	**194,494**	**206,166**
Liabilities					
Deposits held	365	365	365	365	365
Advances received	0	0	0	0	0
Government securities(a)	61,452	59,284	59,106	60,932	60,633
Loans	5,595	5,164	5,190	5,212	4,912
Other borrowing	224	189	158	124	90
Superannuation liability	91,071	95,578	98,801	101,997	105,168
Other employee entitlements and provisions	7,605	7,812	7,918	8,080	8,266
Other non-equity liabilities	28,416	29,699	30,436	31,493	32,655
Total liabilities	**194,727**	**198,089**	**201,974**	**208,201**	**212,088**
Net worth(c)	**-34,126**	**-27,779**	**-20,421**	**-13,708**	**-5,922**
Net debt(d)	16,328	6,080	-14,031	-34,649	-56,389

(a) For 2005-06 and the forward years, the netting of assets — investments, loans and placements — and liabilities — government securities — has been removed so that both lines are now reported on a gross basis.
(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) Net worth is calculated as total assets minus total liabilities.
(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 B3: Australian Government general government sector cash flow statement[(a)]

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Cash receipts from operating activities					
Taxes received	186,205	197,829	204,975	214,781	225,895
Receipts from sales of goods and services	5,015	5,165	5,385	5,526	5,565
Grants and subsidies received	0	0	0	0	0
Interest receipts	1,460	1,828	2,649	3,783	4,789
Dividends	3,808	3,632	2,952	2,357	1,852
GST input credits received by general government	2,908	2,844	2,882	2,976	3,018
Other receipts	2,849	2,926	2,875	2,851	2,938
Total operating receipts	**202,246**	**214,224**	**221,717**	**232,275**	**244,057**
Cash payments for operating activities					
Payments for goods and services	-48,518	-51,455	-53,809	-56,082	-57,310
Grants and subsidies paid	-45,200	-49,195	-50,285	-52,167	-52,753
Interest paid	-3,856	-4,587	-3,808	-3,534	-3,450
Personal benefit payments	-73,664	-76,487	-82,415	-88,071	-96,604
Salaries, wages and other entitlements	-16,508	-17,102	-17,371	-18,002	-18,693
GST payments by general government to taxation authority	-120	-120	-122	-123	-124
Other payments for operating activities	-2,988	-3,079	-2,635	-2,730	-2,958
Total operating payments	**-190,855**	**-202,026**	**-210,443**	**-220,710**	**-231,892**
Net cash flows from operating activities	**11,391**	**12,198**	**11,273**	**11,565**	**12,165**
Cash flows from investments in non-financial assets					
Sales of non-financial assets	416	291	175	250	188
Purchases of non-financial assets	-2,579	-3,102	-2,549	-2,313	-2,011
Net cash flows from investments in non-financial assets	**-2,163**	**-2,812**	**-2,374**	**-2,063**	**-1,823**
Net cash flows from investments in financial assets for policy purposes	**-1,317**	**-1,518**	**9,286**	**9,054**	**9,022**
Cash flows from investments in financial assets for liquidity purposes					
Increase in investments	-7,456	-7,217	-18,306	-20,751	-19,023
Net cash flows from investments in financial assets for liquidity purposes	**-7,456**	**-7,217**	**-18,306**	**-20,751**	**-19,023**
Cash flows from financing activities					
Advances received (net)	0	0	0	0	0
Borrowing (net)	188	-1,579	-30	1,928	-481
Deposits received (net)	0	0	0	0	0
Other financing (net)	-1,306	288	322	18	72
Net cash flows from financing activities	**-1,118**	**-1,291**	**291**	**1,946**	**-408**
Net increase/decrease in cash held	**-663**	**-639**	**171**	**-249**	**-67**
Net cash from operating activities and investments in non-financial assets	**9,227**	**9,387**	**8,899**	**9,502**	**10,342**
Finance leases and similar arrangements(b)	-7	-4	-23	-5	-4
GFS cash surplus(+)/deficit(-)	9,221	9,383	8,876	9,497	10,338
less Future Fund earnings	0	462	943	997	1,054
Equals underlying cash balance	**9,221**	**8,921**	**7,933**	**8,500**	**9,284**
plus net cash flows from investments in financial assets for policy purposes	-1,317	-1,518	9,286	9,054	9,022
plus Future Fund earnings	0	462	943	997	1,054
Equals headline cash balance	**7,904**	**7,865**	**18,163**	**18,550**	**19,360**

(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)

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Opening net worth	**-37,803**	**-34,126**	**-27,779**	**-20,421**	**-13,708**
Opening net worth adjustments(a)	-1,741	0	0	0	0
Adjusted opening net worth	**-39,544**	**-34,126**	**-27,779**	**-20,421**	**-13,708**
Change in net worth from operating transactions	**7,655**	**8,430**	**8,076**	**8,005**	**8,758**
Change in net worth from other economic flows					
Revaluation of equity(b)	1,301	261	322	-19	4
Net writedowns of assets (including bad and doubtful debts)	-2,226	-1,447	-1,650	-1,693	-1,306
Assets recognised for the first time	23	94	80	58	58
Liabilities recognised for the first time	0	0	0	0	0
Actuarial revaluations	-937	0	0	0	0
Net foreign exchange gains	-384	0	0	0	0
Net swap interest received	180	102	96	77	70
Market valuation of debt	-195	371	303	257	148
Other economic revaluations(c)	2	-1,463	131	29	53
Total other economic flows	**-2,236**	**-2,083**	**-717**	**-1,291**	**-973**
Closing net worth	**-34,126**	**-27,779**	**-20,421**	**-13,708**	**-5,922**

(a) Decrease in net worth arising from a change in recognition of family tax benefits and other expenses from a cash to an accrual basis.

(b) Revaluations of equity reflect 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) Largely reflects revaluation of assets and liabilities and Australian Equivalents to International Financial Reporting Standards adjustments.

APPENDIX C: SENSITIVITY OF EXPENSES AND REVENUE TO ECONOMIC DEVELOPMENTS

A guide to the sensitivity of the forward estimates of expenses and revenue due to variations in economic parameters in 2005-06 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 expenses and revenue to changes in economic parameters

	2005-06 $m	2006-07 $m	2007-08 $m	2008-09 $m
Expenses				
Prices	1,310	860	900	920
Wages	120	410	450	470
Unemployment benefit recipients	250	250	260	270
Safety Net Adjustment	40	150	240	340
Revenue				
Prices	50	110	110	110
Wages	1,570	1,690	1,800	1,930
Employment	1,080	1,150	1,240	1,320
Private final demand	280	290	300	300
Profit	340	560	610	650

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 of the parameters will lead to a reduction in expenses.

Prices

All price growth rates are assumed to change by one percentage point in the September quarter 2005 and to remain unchanged subsequently, with wage and salary growth rates left unchanged through the Budget and forward years.

- The effect of a change in prices is due to the indexation of Australian Government expenses and a large one-off impact on superannuation liabilities in 2005-06, which in turn impacts on the superannuation interest expense.

Wages

All wage and salary growth rates are assumed to change by one percentage point in the September quarter 2005 and to remain unchanged subsequently, with all price growth rates left unchanged through the Budget and forward years.

- The effect of a change in wage and salary growth rates is largely due to the Government's commitment to maintain selected pensions at a minimum of 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 5 per cent in the Budget year and the following years.

Safety Net Adjustment

The Safety Net Adjustment determined by the Australian Industrial Relations Commission is assumed to change by $2 per week in 2005-06 and the following years.

- About $50 billion of expenses in 2005-06, 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 the Consumer Price Index and the Safety Net Adjustment.

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 quarter 2005, with wage deflators left unchanged.

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

Wages

All wage and salary growth rates are assumed to change by one percentage point from the beginning of the September quarter 2005, with price deflators left unchanged.

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

Employment

The level of employment is assumed to change by one percentage point from the beginning of the September quarter 2005, with no change in the composition of employment.

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

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 quarter 2005, 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 quarter 2005.

- 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 Australian economy is expected to record solid growth in real GDP in 2005-06 after passing through a soft patch in 2004-05. Strong world demand for commodities will benefit Australia through increasing export volumes and higher terms of trade, both of which will support strong growth in national income. Gross national expenditure is forecast to grow at more moderate rates in 2004-05 and 2005-06 after a period of exceptionally strong growth in recent years. Employment growth is forecast to ease towards trend in 2005-06, while inflation is expected to remain moderate.

OVERVIEW

The rebalancing of **economic growth** in Australia from domestic to external sources that was foreshadowed in the 2004-05 Budget is occurring slowly. Real GDP growth is forecast to be 2 per cent in 2004-05, lower than the forecast presented in the *Mid-Year Economic and Fiscal Outlook 2004-05* (MYEFO). Dwelling investment and consumption growth slowed in the second half of 2004, after having experienced rapid growth in recent years. Export growth has also been slower than expected given the strength of world economic conditions. This largely reflects a continued high exchange rate, and the long lead times required to increase production in the mining sector and to expand export capacity. Despite slow growth in export volumes, high commodity prices provided a substantial boost to domestic income in 2004-05.

In 2005-06, the rebalancing of growth from domestic to external sources is expected to continue, with economic growth forecast to strengthen to 3 per cent. Gross national expenditure is expected to grow solidly, albeit slower than the very high average rate seen since 2001-02. Growth in household consumption and dwelling investment is expected to moderate, while business investment and public demand are forecast to grow at around trend rates.

Exports are expected to be an important contributor to growth in 2005-06. The mining sector invested around A$20 billion over 2003 and 2004 to boost capacity, which should be reflected in significant growth in non-rural commodity exports over the coming year. Rural exports are forecast to grow modestly in 2005-06, with growth restrained by a smaller grain harvest. Solid growth is expected in other categories of exports, supported by a strong world economy, but still affected by the high exchange rate.

The current account deficit (CAD) is forecast to narrow in 2005-06. The combination of increased export volumes and prices should lead to a markedly smaller trade deficit. The reduction in the CAD will be somewhat smaller than the reduction in the trade deficit because part of the additional income from higher commodity prices will accrue to foreigners. Payment of additional income abroad will increase Australia's net income deficit.

Employment growth is forecast to ease towards trend in 2005-06, following the period of slower GDP growth in 2004. Unemployment is expected to remain around its current rate through 2005-06. Wage growth is forecast to remain moderate although, with the unemployment rate at a 28-year low, some localised wage pressures have begun to appear in particular industries and geographic areas. Inflation is expected to remain moderate in 2005-06.

The **world economy** is forecast to remain strong over the next two years. World economic growth is forecast to be 4¼ per cent in 2005 and 4 per cent in 2006. This is a little below the very brisk growth rate of 5.1 per cent in 2004. High oil prices and the effects of tighter macroeconomic policies, particularly in the United States and China, are contributing to the modest slowing. World inflationary pressures are expected to remain contained. There is little evidence yet that higher commodity prices are leading to significant second-round price increases in the major industrialised countries.

In the domestic economy, **household consumption** growth is expected to moderate to 3¼ per cent in 2005-06, supporting a modest rebuilding of household saving. A substantial slowdown in the accumulation of housing wealth, following several years of very strong growth, and the recent increase in official interest rates will restrain consumption. High petrol prices are also expected to continue to retard consumption growth. Partly offsetting these factors, consumption will be supported by the effects of past increases in non-housing wealth, particularly share prices, and continued solid growth in household incomes. Household incomes will benefit from continued employment growth and income tax cuts, although some portion of the tax cuts is likely to be saved.

Dwelling investment fell in the second half of 2004 after growing by almost 50 per cent in the three years to 2003-04. Dwelling investment is expected to fall by 2 per cent in 2005-06 as the recent increase in official interest rates and falls in house prices combine to dampen activity, particularly in the investor sector. However, the current housing downturn is expected to be muted compared with past cycles, with dwelling investment supported by a strong labour market and solid underlying demand for new dwellings.

Business investment is expected to again grow solidly in 2005-06. The growth in business investment in recent years has been broadly based, with the mining sector a particularly important contributor. The investment environment remains favourable, with high capacity utilisation, a relatively low cost of capital and very strong corporate balance sheets.

Public final demand should grow at a solid rate of 3¾ per cent in 2005-06, with strong growth in public investment and slowing growth in public consumption.

Australia's **net export** position is expected to strengthen in 2005-06, reflecting a rebalancing of growth from domestic to external sources. Exports are forecast to grow by 7 per cent in 2005-06, after a period of sluggish growth since 2001-02. Modest growth in exports through this period has reflected the various economic shocks buffeting the Australian economy, a slow investment response to rising terms of trade and the high exchange rate since late 2003. Growth in **imports** is expected to ease to 8 per cent in 2005-06, in line with moderating growth in gross national expenditure.

The increase in world demand for raw materials, and limited world supply response, has resulted in markedly higher commodity prices (see Box 1). As a result, Australia's **terms of trade** are forecast to increase by 12¼ per cent in 2005-06, building on the 9¾ per cent increase expected for 2004-05. With an increase in the terms of trade and stronger export growth, the **current account deficit** is expected to narrow to 5¼ per cent of GDP in 2005-06.

Higher export prices are likely to result in very strong **nominal GDP** growth. Nominal GDP is forecast to grow by 7½ per cent in 2005-06. Corporate profits are likely to increase significantly in 2005-06 as mining companies benefit from higher export prices.

Employment growth is expected to moderate to 1¾ per cent in 2005-06, in line with recent slower GDP growth. The unemployment rate fell to 5.1 per cent in December 2004, the lowest rate in close to three decades. The unemployment rate is forecast to remain around 5 per cent, on average, over 2005-06. Rates of workforce participation are expected to remain broadly unchanged, albeit at high levels.

Inflation is expected to remain within the target band, with the Consumer Price Index forecast to increase by 2¾ per cent in 2005-06 as petrol prices remain high in the near term. This pressure is expected to moderate through 2005-06, with inflation forecast to be 2½ per cent through the year to the June quarter 2006. The cyclical slowing in labour productivity in 2004-05 is expected to have only a modest flow-through to consumer prices. There is no evidence that higher oil and other commodity prices are leading to significant second-round increases in consumer prices, although this remains a risk.

Wage growth is expected to increase modestly in 2005-06, with the Wage Price Index forecast to grow by 4 per cent. With the unemployment rate at a 28-year low, some localised wage pressures have appeared in particular regions and occupations. However, relative wage adjustment is an important signalling mechanism in a high employment economy and there is little evidence of generalised wage pressures or skill shortages. This is likely to remain the case as the economy passes through a period of more moderate employment growth.

A key **risk** to the economic outlook is the effect of the significant rise in Australia's export prices, which is forecast to take the terms of trade to their highest level since the early 1950s. The way in which mining companies respond to this additional income — by investing it, saving it or returning it to shareholders — will be important for the outlook.

Higher export prices are expected to have only a limited effect on household finances, primarily through equity holdings in mining companies. It is unlikely that higher export prices will result in significant growth in wages outside the mining sector itself, or have a major impact on aggregate employment growth across the economy. However, if these effects are greater than anticipated, then it is possible that resulting higher household incomes would lead to higher household consumption than currently forecast.

Higher export prices are not expected to result in a significant increase in investment by mining companies in 2005-06 over that which has already been announced. While it is possible that companies might invest more quickly than anticipated in response to high commodity prices, this upside risk is offset somewhat by the likelihood that commodity prices will fall beyond the present forecast period. As a substantial increase in supply is forthcoming from more recent investment in many countries, it is likely that commodity prices will retrace significantly in the medium term. This raises some issues for the projections of nominal GDP in 2006-07 and beyond. These issues are discussed in more detail in Box 7.

High commodity prices, particularly high oil prices, also present a downside risk for economic growth. Oil prices directly affect petrol prices and indirectly affect the prices of many other goods and services. High prices for iron ore affect steel prices and the cost of engineering and building construction. If oil prices increase further, this would present a downside risk to the forecasts for GDP growth in the near term. In the medium term, Australia would benefit from higher commodity prices as a net energy and mineral exporter and this would most likely boost economic growth.

Previous budget discussions of the economic outlook have identified a risk to consumption growth from the increasing level of household debt. In aggregate, there is no evidence that households are having difficulties servicing their current debt and, with consumption and dwelling investment both expected to slow, it is likely that households will take on debt at a slower rate through 2005-06. Nevertheless, there remains a possibility that households will seek to rebuild their saving to a greater extent than anticipated, leading to lower consumption growth than forecast.

While the risks around developments in the housing sector appear to have abated somewhat since the 2004-05 Budget, there remain concerns in particular market segments. Overall, it appears that house prices fell modestly over 2004. The likely outcome is that house prices will remain broadly flat in 2005-06 as the housing market continues to adjust to lower rates of turnover. While this adjustment is expected to be orderly, if house prices were to fall further then this would put downward pressure on consumption growth.

With the unemployment rate at its lowest level in a generation, there is a risk that the tight labour market could lead to wage increases across the economy that are greater than is justified by productivity growth. This would put upward pressure on unit labour costs and inflation. Measures to increase workforce participation outlined in this Budget should help to reduce this risk over the medium term.

As is normal practice, the forecasts for the rural sector are predicated on an assumption that average seasonal conditions will prevail in 2005-06. The actual timing and distribution of rainfall through 2005 will have an important influence on rural production and exports in 2005-06, as will the lingering effects of dry weather in recent years.

The near-term risks for the world economic outlook appear to be balanced. But some medium-term downside risks remain, largely centred on different growth profiles across major economies, and associated fiscal and current account imbalances. While these imbalances may persist for some time without significant adverse consequences, they increase the vulnerability of the world economy to destabilising changes in financing flows.

Table 1: Domestic economy forecasts(a)

	Outcomes(b) 2003-04 year average	Estimates 2004-05 year average	Forecasts 2005-06 year average	Forecasts Four quarters to June 2006
Panel A - Demand and output(c)				
Household consumption	5.6	4	3 1/4	3 1/2
Private investment				
Dwellings	7.3	-2	-2	1
Total business investment(d)	9.4	8	6	6
Non-dwelling construction(d)	12.5	2	2	2
Machinery and equipment(d)	7.8	11	7	7
Private final demand(d)	6.2	3 3/4	3 1/2	3 3/4
Public final demand(d)	3.8	6	3 3/4	1 1/4
Total final demand	5.7	4 1/4	3 1/2	3 1/4
Change in inventories(e)				
Private non-farm	0.0	- 1/4	1/4	1/4
Farm and public authorities(f)	0.6	- 1/4	0	0
Gross national expenditure	6.2	3 1/2	3 3/4	3 1/2
Exports of goods and services	1.6	2	7	7
Imports of goods and services	12.4	10	8	8
Net exports(e)	-2.4	-2	-1	- 3/4
Gross domestic product	4.1	2	3	3 1/4
Non-farm product	3.3	2 1/4	3	2 3/4
Farm product	35.8	-8	5	17
Panel B - Other selected economic measures				
External accounts				
Terms of trade	7.0	9 3/4	12 1/4	6
Current account balance				
$billion	-47.4	-56 1/4	-48	
Percentage of GDP	-5.8	-6 1/2	-5 1/4	
Labour market				
Employment (labour force survey basis)	1.8	2 3/4	1 3/4	1 1/2
Unemployment rate (per cent)(g)	5.8	5 1/4	5	5
Participation rate (per cent)(g)	63.5	63 3/4	63 3/4	63 3/4
Prices and wages				
Consumer Price Index	2.4	2 1/2	2 3/4	2 1/2
Gross non-farm product deflator	3.6	4	4 1/2	3 1/2
Wage Price Index	3.6	3 3/4	4	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, 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 2006.
Source: Australian Bureau of Statistics (ABS) Cat. No. 5206.0, 5302.0, 6202.0, 6345.0, 6401.0, unpublished ABS data and Treasury.

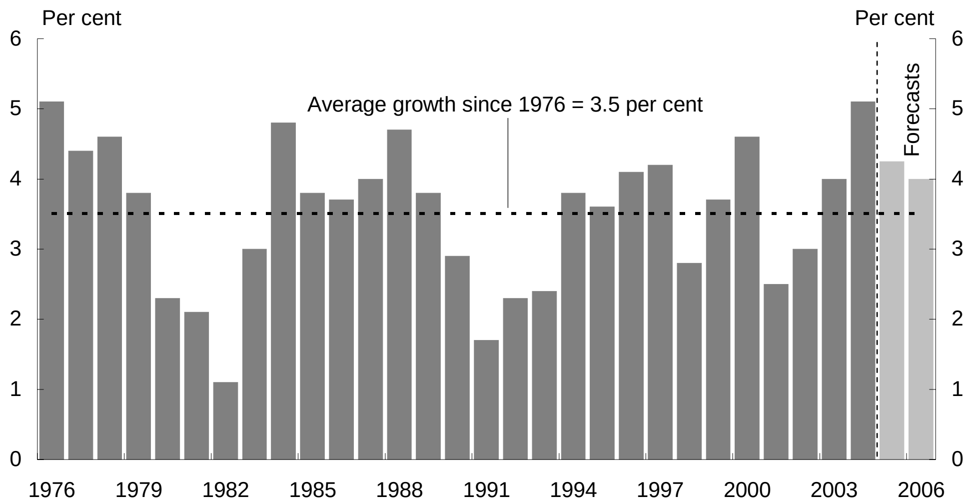
THE OUTLOOK FOR THE INTERNATIONAL ECONOMY

The world economy grew by 5.1 per cent in 2004, its fastest rate in close to 30 years and around ½ of a percentage point higher than expected at MYEFO. Strong growth was recorded across most regions, with emerging markets, in particular, benefiting from low world interest rates combined with strong demand and high prices for their commodity exports.

After peaking in the early part of 2004, world growth eased over the remainder of the year and into 2005 as the effects of high oil prices and tighter policy, particularly in the United States and China, took hold. However, with conditions in the world economy expected to remain favourable, growth is expected to stabilise at the still-solid rates recorded in the latter part of 2004, although the pattern of growth across countries is likely to be more unbalanced than previously anticipated.

World GDP growth is forecast to ease to 4¼ per cent in 2005 and 4 per cent in 2006 (see Chart 1). Growth in Australia's major trading partners is expected to ease from 4.9 per cent in 2004 to around trend rates of 3¾ per cent in 2005 and 2006.

Chart 1: World GDP growth(a)



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

World inflationary pressures are expected to remain muted. To date there has been little evidence of significant second-round effects from higher oil and other commodity prices in the major industrialised economies. In part, this reflects competitive product and labour markets and the success of macroeconomic policy in establishing well-anchored inflation expectations.

Risks to the outlook appear broadly balanced in the near term, although the persistence of global imbalances — reflected in current account positions — has increased the underlying vulnerability of the world economy over the medium term.

A downside risk to world growth stems from the increasingly unbalanced nature of the current expansion. The easing of world growth in the second half of 2004 was particularly evident in Japan and the euro area, while other major regions continued to grow strongly. This heightens the world economy's exposure to developments in a few key economies, particularly the United States and China.

Unbalanced growth, if sustained, is likely to exacerbate already large current account imbalances around the world, increasing the risk of a disorderly adjustment in financial markets. The US current account deficit was a record US$666 billion in 2004, equivalent to two-thirds of the aggregate current account surpluses in the rest of the world. These imbalances are attributable to a number of factors, including insufficient saving in the United States (particularly by the public sector), disappointing growth in Japan and the euro area (reducing their attractiveness relative to the United States as a destination for global capital), and a degree of under-investment in some East Asian countries (resulting in large and continuing current account surpluses in that region).

A gradual and orderly unwinding of these imbalances remains the most likely path of adjustment in the medium term. This would require a combination of fiscal consolidation in the United States, further US dollar depreciation and an improvement in the growth performance of Japan and the euro area. The depreciation of the dollar to date has been relatively steady and the normalisation of interest rates in the United States should also provide impetus for increased private saving, particularly if house price growth slows.

While the policy prescriptions required to rebalance the world economy are understood, little progress has been made in implementing them, suggesting that imbalances will continue to deepen in the near term. The longer policy action is deferred, the more exposed the United States and the world economy will be to a sudden change in sentiment regarding the relative risk and reward from holding US dollar assets. Such a change in investor sentiment could result in an abrupt and disruptive adjustment to exchange rates and interest rates.

Of more immediate concern are continued high and volatile oil prices. While the benchmark West Texas Intermediate price has moderated from the record nominal high of over US$57 per barrel in early April, it remains high by historical standards. To date, high oil prices have had a limited impact on world economic growth and core inflation. However, with oil prices expected to remain high in the medium to longer term, there remains the possibility that they will feed into inflation expectations more than currently expected. This risk is greater given that excess capacity in some major economies, including the United States, has been largely unwound over 2004. A sharp increase in inflation expectations could be particularly damaging for world growth given the unusually low level of US long-term interest rates and historically low risk premia on corporate and emerging market debt.

On the upside, world growth over the past few years has consistently been stronger than anticipated. The factors that have underpinned this — accommodative monetary policy, healthy corporate balance sheets and benign financial market conditions — remain in place. As a result, the current economic expansion could prove more resilient than currently envisaged.

Table 2: International GDP growth forecasts[(a)]

	2003 Actual	2004 Estimate	2005 Forecast	2006 Forecast
United States	3.0	4.4	3 1/2	3 1/2
Euro area[(b)]	0.5	1.8	1 1/2	2
Japan	1.4	2.6	1 1/4	2
China	9.3	9.5	8 1/2	8
Other East Asia[(c)]	3.6	6.1	4 3/4	5
Major trading partners	3.4	4.9	3 3/4	3 3/4
OECD	2.2	3.4	2 3/4	2 3/4
World	4.0	5.1	4 1/4	4

(a) World, OECD and euro area growth rates are calculated using GDP weights based on purchasing power parity. Calculations for major trading partners and other East Asia use export trade weights.
(b) 2004 estimate adjusted for the number of working days.
(c) Other East Asia consists of Korea, Singapore, Taiwan, Hong Kong, Indonesia, Malaysia, Thailand, and the Philippines.
Source: Various national statistical authorities, International Monetary Fund and Treasury.

Economic growth in the **United States** evolved largely as expected through 2004. Growth remained solid, but moderated as excess capacity in the economy narrowed and policy settings moved toward more neutral levels. Concerns about the labour market, which had been slow to recover from the 2001 recession, abated somewhat, with solid, albeit intermittent, gains in employment.

Domestic demand in the United States is expected to rebalance progressively away from household consumption toward business investment in 2005. The business sector, which has rebuilt its financial position in recent years, is expected to continue to invest strongly in 2005 and 2006. Conversely, households, which have spent well ahead of growth in income, driving the household saving rate to record lows, are expected to consolidate their finances. While household income will be supported by the ongoing recovery in the labour market, the high level of household debt makes consumption sensitive to increases in interest rates and fluctuations in income. A risk remains that US households may move abruptly to consolidate their financial position, particularly if financial market conditions tighten sharply.

Inflationary pressures in the United States are expected to remain in check over the forecast period, with inflation expectations well-anchored and the monetary tightening cycle now well underway. However, with the labour market expected to tighten further, productivity growth slowing from cyclical peaks, and higher oil and other commodity prices, growth in unit labour costs could be stronger than expected.

After growing strongly toward the end of 2003 and in the early part of 2004, **Japan's** economy contracted in the middle of 2004 and posted only moderate growth in the December quarter. However, there are concerns about the quality of national accounts data, which have been subject to frequent and large revisions. Partial data indicate a more moderate easing in growth over the course of 2004.

Fundamentals in the Japanese economy have improved significantly in recent years, suggesting a continuation of growth in the period ahead. Structural reforms have improved business sentiment and corporate profits and the unemployment rate has fallen to near six-year lows. Deflation, which has weighed on consumer and business confidence in recent years, eased in 2004 and is expected by the Bank of Japan to end in early 2006.

China's economy grew at its fastest rate in almost a decade in 2004, contributing strongly to world growth and demand for commodities (see Box 1). However, concerns remain about the sustainability of the expansion, and the efficiency of the investment underpinning it. Authorities continued to use a combination of market instruments and administrative controls to tighten monetary conditions over the course of 2004 and there are signs that these measures are having an effect. While investment remains unsustainably high as a share of GDP, it has moderated somewhat. Growth in other key indicators, including industrial production, money supply and credit, eased in 2004. These data suggest that economic growth will slow to a more sustainable rate of around 8 per cent, although there remains considerable uncertainty about the timing and extent of the slowing.

The strength of the Chinese economy has led to external calls for greater flexibility in its exchange rate, particularly from the United States. However, a more flexible Chinese exchange rate is likely to have only a limited impact on global imbalances. Broader liberalisation of the capital account should be approached cautiously and coincide with a further strengthening in the Chinese financial system. These reforms, if complemented by ongoing structural reforms elsewhere in the economy, would provide a sound footing for balanced growth in the long term.

The **rest of East Asia** also grew strongly in 2004, underpinned by strong external and domestic demand. However, growth appears to have peaked, with regional economies (except Indonesia) expected to grow at a slower pace in 2005 and 2006. This reflects easing export growth due to more moderate world demand and a slowing in the global information and communication technology cycle. That said, the outlook for domestic demand remains positive, and should support still-solid growth in the region. The notable exception is Korea, where domestic demand remains weak following the bursting of the household credit bubble in 2003, although more recently, there have been signs of a pick-up in consumer and business confidence.

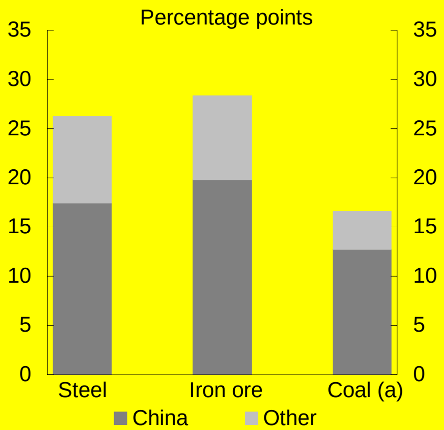
Box 1: World demand and commodity prices

The world economy grew rapidly in 2004. The composition of growth was weighted heavily towards the United States and China. Together these two countries contributed 2.2 percentage points to world growth of 5.1 per cent in 2004.

The United States and China are major commodity users. Their strong output growth saw a significant increase in demand for commodities such as oil, iron ore and coal.

In particular, China's emergence as a major commodity importer has had a significant impact. For example, over the period 2001 to 2004, China was responsible for 70 per cent of the world increase in iron ore consumption (Chart A).

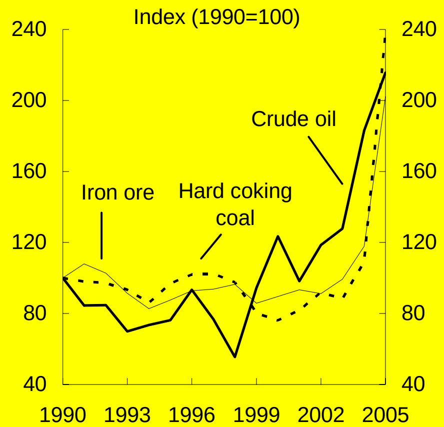
Chart A: Growth in world commodity consumption, 2001 to 2004



(a) Coal consumption growth from 2001 to 2003.
Source: AME Mineral Economics and BP Statistical Review of World Energy.

The rapid rise in commodity prices (Chart B) has generated significant benefits for commodity exporters like Australia, Canada, the Middle East, Russia and South Africa.

Chart B: Commodity prices (US$)[(a)]



(a) Year from April to March.
Source: ABARE, Thomson Financial and Treasury.

Investment in exploration and production has increased in response to the sustained commodity price rise. As a consequence, despite continued strong demand, commodity prices are likely to ease somewhat as additional world production comes on stream. However, if world demand were to falter, there is a risk that commodity prices could fall further than anticipated.

Growth in the **euro area** slowed sharply in the second half of 2004, with the combination of euro appreciation and high oil prices undermining the modest recovery that had taken place since the middle of 2003. Looking forward, growth is forecast to pick-up from recent levels, albeit at a more moderate pace than previously expected. The favourable world economic outlook will continue to underpin exports, despite the appreciation of the euro. Solid corporate profitability should see an improvement in the labour market, supporting a rebound in consumer spending.

The risks to this outlook, however, are skewed to the downside and reflect long-standing structural weaknesses. While some progress has been made on pension, health care and labour market reform in Germany and France, and on pension reform in Italy, more needs to be done. Reforms to lift labour force participation and productivity are particularly important in the face of rapidly ageing populations.

The **United Kingdom** economy grew strongly over the course of 2004, although recent data suggest that monetary policy tightening during that year is beginning to have an effect. The outlook is for growth to remain steady at recent, more moderate, rates.

THE OUTLOOK FOR THE DOMESTIC ECONOMY

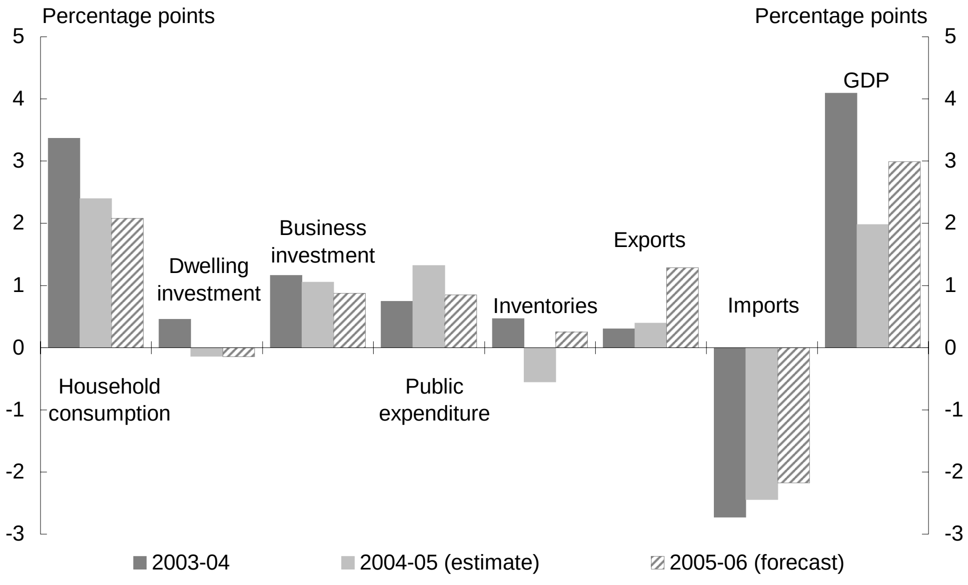
Key assumptions

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 64). Interest rates are assumed to remain at current levels. World oil prices (West Texas Intermediate) are assumed to remain broadly unchanged through 2005-06, consistent with market expectations. The farm sector forecasts are based on an assumption of average seasonal conditions in 2005-06.

Demand and output

The rebalancing of growth from domestic to external sources that was foreshadowed in the 2004-05 Budget is occurring slowly and remains the most likely path for the economy in the period ahead. In the second half of 2004, gross national expenditure growth slowed, but export growth failed to pick up significantly, leading to a slowing in GDP growth from the very strong rates of recent years. GDP growth is expected to be 2 per cent in 2004-05 (see Chart 2). In contrast with moderate GDP growth, national income is expected to grow strongly, reflecting increased export prices.

Chart 2: Contributions to GDP growth(a)(b)



(a) Excluding transfers of second-hand assets from the public sector to the private sector.
(b) All charts in the domestic economy outlook section use seasonally adjusted data unless otherwise specified.
Source: ABS Cat. No. 5206.0 and Treasury.

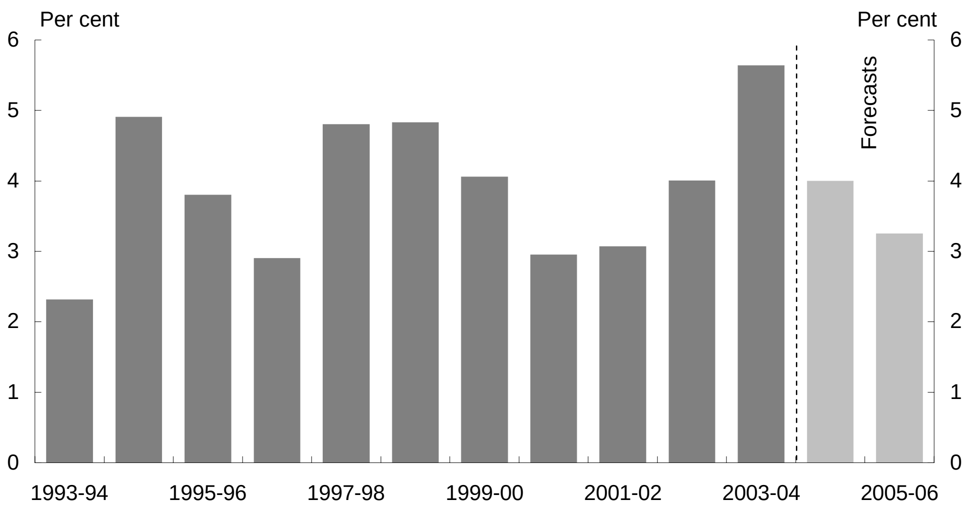
GDP growth is forecast to strengthen to 3 per cent in 2005-06. Household consumption is expected to make a smaller contribution to growth, while dwelling investment is again expected to detract from growth after the high level of construction activity in recent years. The contribution to growth from business investment is expected to remain solid. Public expenditure will contribute solidly across the forecast period. Imports are expected to detract less from growth, broadly in line with the developments in the domestic economy. Exports are forecast to make a larger contribution to growth in 2005-06, particularly as additional capacity comes on stream in the resources sector.

Non-farm GDP is forecast to grow by 2¼ per cent in 2004-05, strengthening to 3 per cent in 2005-06. Farm GDP is expected to fall by 8 per cent in 2004-05, largely reflecting generally dry conditions and the late arrival of spring rains in some areas, before increasing by 5 per cent in 2005-06 on the assumption of average seasonal conditions.

Household consumption

Household consumption is forecast to grow by 3¼ per cent in 2005-06, down from the 4 per cent growth expected for 2004-05 and below the rapid rates of growth recorded in recent years (see Chart 3).

Chart 3: Growth in consumption

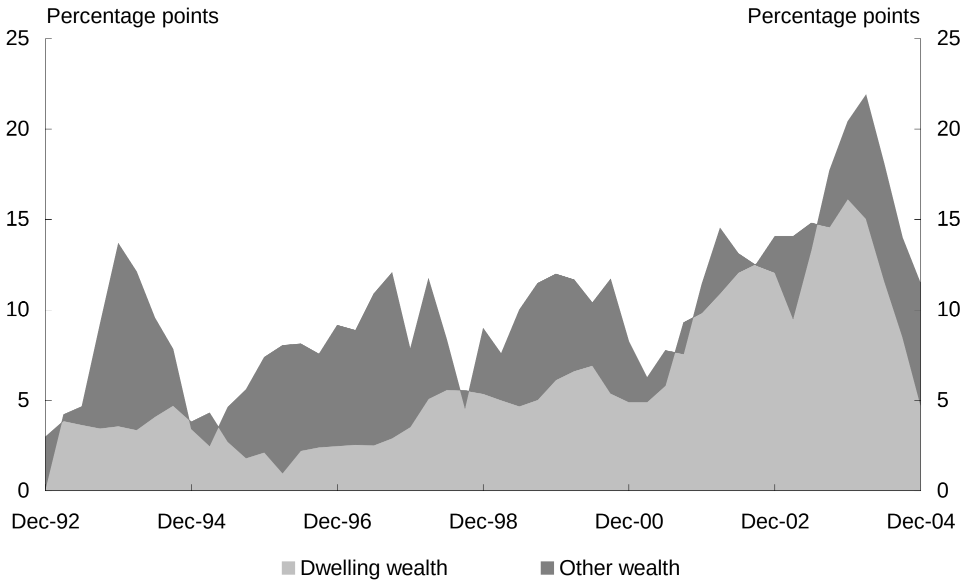


Source: ABS Cat. No. 5206.0 and Treasury.

Household income has grown steadily over the past decade, supported by increases in employment and real wages. However, the growth in income over the past decade has been insufficient to explain all of the increase in consumption. The other major contributing factor has been an increase in household wealth. Through the 1990s, higher wealth generally took the form of higher equity prices, although higher house prices have been the more important factor in recent years (see Chart 4). These increases in wealth have seen consumption grow by more than income on average and, as a result, the household saving ratio has fallen. Australia's changing demographic profile, and the lower demand for precautionary savings in a stable and prosperous economic environment, may also have affected saving behaviour in the past decade (see Box 4).

Households are expected to increase their consumption by less than the increase in their income over 2004-05 and 2005-06. Accordingly, the rate of household saving is expected to increase, albeit by a modest amount. Recent data provide evidence that a rebuilding of household saving may have already commenced. Household nominal net disposable income increased by 6.9 per cent through the year to the December quarter 2004, while nominal consumption expenditure increased by a more moderate 5.4 per cent. It appears that some households saved the additional income from the 2004-05 Budget measures that reduced income taxes and increased the financial assistance to families with children. This trend is likely to continue with further income tax cuts and measures to support saving in the 2005-06 Budget.

Chart 4: Contributions to growth in nominal household wealth[(a)]



(a) Percentage point contribution to through-the-year growth.
Source: Treasury.

The expected easing in household consumption, and the consequent increase in saving, is partly the result of the substantial slowdown in house price growth over the past year. Although there can be large differences between the various measures of house prices, this slowdown was evident across all of the major data sources. For example, the Australian Bureau of Statistics' measure of established house prices grew by 18.9 per cent over 2003, but only by 2.7 per cent over 2004. If households seek to rebuild their saving more quickly in response to these developments, then household consumption growth would be lower.

One factor that has offset the lower growth in housing wealth is the large growth in non-dwelling wealth over the past few years. The ASX200 share price index increased by more than 30 per cent in the two years to April 2005. This increase partly reflects the improved prospects of resource companies following substantial increases in world commodity prices — the resources component of the ASX200 increased by more than 80 per cent over the same two-year period.

Aside from lower growth in housing wealth, other factors that are likely to slow household consumption over the forecast period are the increase in official interest rates in March 2005 and high petrol prices. The forecasts assume that oil prices remain broadly unchanged over 2005-06 and, therefore, that petrol prices stabilise. But there is a risk that oil prices increase and put further pressure on consumption spending.

Dwelling investment

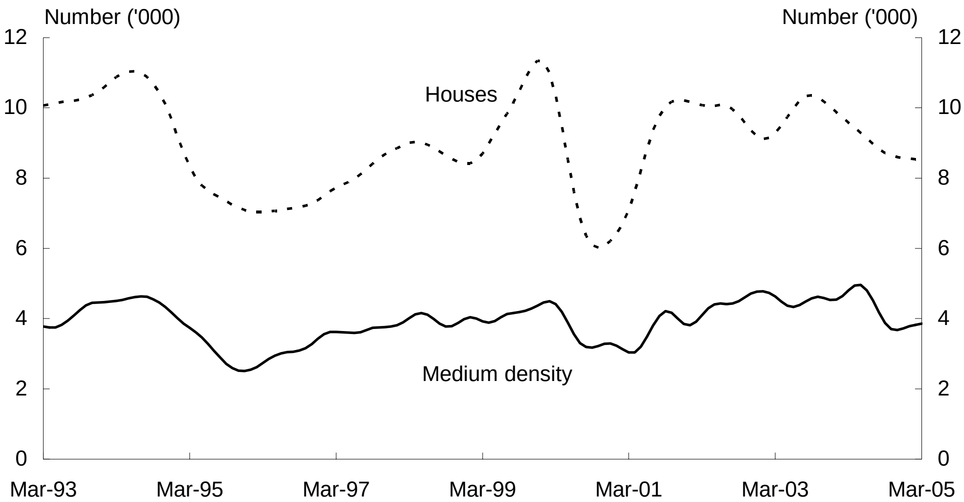
Dwelling investment is forecast to fall by 2 per cent in both 2004-05 and 2005-06, after very strong growth over the previous three years. Dwelling investment fell in the second half of 2004 and forward indicators of activity in the housing sector, such as dwelling approvals, suggest that this modest downward trend will continue in coming months (see Chart 5).

Other partial housing sector indicators point to lower activity. In late 2004 and early 2005, the number of monthly finance commitments for the construction or purchase of new dwellings by owner-occupiers was running around 15 per cent below its most recent peak in October 2003. Much of the speculative activity in the investor market also appears to have passed, with the value of investor finance falling significantly over the same period.

Thus far, the current housing cycle is unwinding in an orderly manner, with a gradual fall in housing activity levels across much of the country and house prices stabilising or falling a little. The risk of a sharp fall in house prices appears to have abated since the 2004-05 Budget. However, the rental yields on investment properties are still very low, suggesting that house prices may fall further in real terms. It seems likely that this adjustment will continue to occur gradually, without causing significant disruption to household finances. However, there remains a risk that a prolonged period of falling or flat house prices may lead households to rein in consumption expenditure more than expected.

There is no evidence of a widespread oversupply of new housing. Consistent with favourable economic conditions, the current downturn in housing activity is expected to be relatively shallow, although it is likely that medium density construction activity in the larger cities will continue to fall through 2005-06.

Chart 5: Private dwelling approvals



Source: ABS Cat. No. 8731.0 (trend data).

Business investment

Businesses are in a good position to undertake additional investment expenditure. Business profits have been strong across most sectors (especially in mining), capacity utilisation is at high levels and the Australian dollar prices of many investment goods have been falling over recent years.

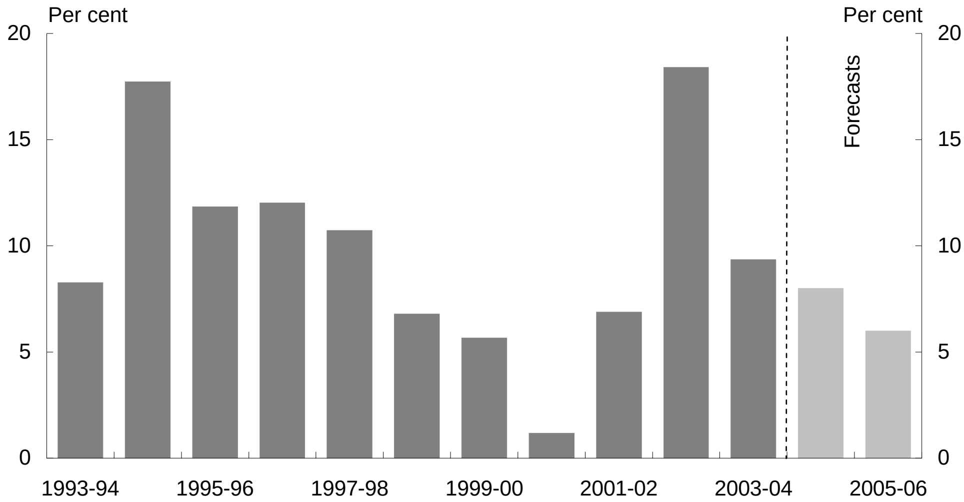
New business investment is forecast to grow by 6 per cent in 2005-06, and remain at a very high level in real terms, having increased by almost 40 per cent in the three years to 2003-04 (see Chart 6). However, falling prices for business investment, particularly for imported machinery and equipment, have meant that nominal business investment has remained broadly constant as a share of nominal GDP.

The mining sector has been an important contributor to business investment over recent years. Data from the Australian Bureau of Statistics' *Survey of New Capital Expenditure and Expected Expenditure* (CAPEX) shows that mining sector investment has been running above A$2 billion a quarter for more than two years, compared with a little above A$1 billion a quarter at the beginning of the decade. Mining sector investment should remain high for some time yet, given strong world demand for commodities.

Investment in non-dwelling construction is expected to grow by around 2 per cent in both 2004-05 and 2005-06. These forecast growth rates represent a moderation from the very strong growth in this category in recent years. Increasing commercial office vacancy rates, a slower rate of commencement of new infrastructure projects and increasing prices for steel and cement will restrain growth in non-dwelling construction. Nevertheless, continuing work on a number of large projects, and supportive conditions for business investment more generally, will help to hold non-dwelling construction at its current high levels.

New machinery and equipment investment is also forecast to remain at high levels in 2005-06 with forecast growth of 7 per cent. The first estimate of investment intentions for equipment, plant and machinery in 2005-06 from the CAPEX survey was 5.2 per cent higher (in nominal terms) than the equivalent estimate for 2004-05. Initial estimates of investment intentions can provide only a broad indication of likely outcomes. Nevertheless, the CAPEX expectations provide early support for continued strong growth in 2005-06.

Chart 6: Growth in new business investment



Source: ABS Cat. No. 5206.0 and Treasury.

Inventories

Changes in inventories are forecast to contribute ¼ of a percentage point to GDP growth in 2005-06, primarily through growth in private non-farm inventories. Despite a positive contribution to growth from inventories, the inventories to sales ratio is expected to fall further in 2005-06 as strengthening export growth boosts overall sales.

Farm and public authority inventories (including the inventories of privatised marketing authorities) are expected to fall in 2004-05, following lower grain production in 2004, and then remain broadly unchanged at this level in 2005-06.

Public final demand

Public final demand is forecast to increase by 3¾ per cent in 2005-06, after expected strong growth of 6 per cent in 2004-05. Public investment expenditure has grown strongly over 2004. In 2005-06, growth in public investment expenditure is expected to slow, as is growth in public consumption.

Net exports and the current account

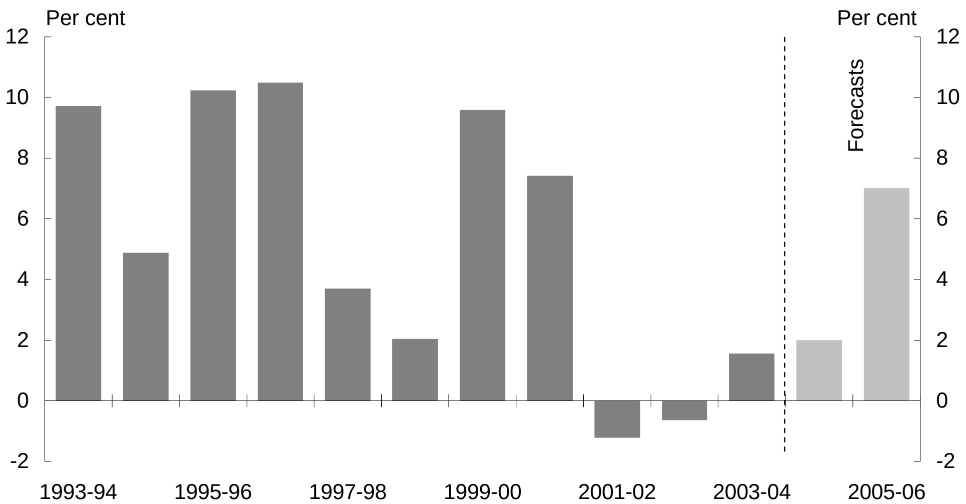
Net exports

Net exports have made a significant detraction from GDP growth over the past three years. Strong growth in gross national expenditure and a high exchange rate have supported import growth in recent years, while export growth has been subdued (see Chart 7). Net exports are expected to detract a further 1 percentage point from GDP growth in 2005-06, an improvement from previous years.

A number of shocks to the economy in the first half of this decade have acted to constrain export growth. The 2002-03 drought and subsequent dry weather conditions affected rural exports, the slowdown in the world economy in 2001 and 2002 weighed on manufactured and service exports, and various health and security concerns have affected international travel and business. The increase in the exchange rate since 2002 has also reduced the price competitiveness of Australian exports.

In volume terms, export growth still remains below what could be expected for this stage of the world economic cycle. An important part of the explanation for this relatively weak growth in export volumes is the long lead times on investment in the mining sector (see Box 2). Around A$20 billion has been invested in new production and transportation capacity in the mining sector over the past two years alone, but non-rural commodity export volumes have remained broadly flat.

Chart 7: Growth in exports

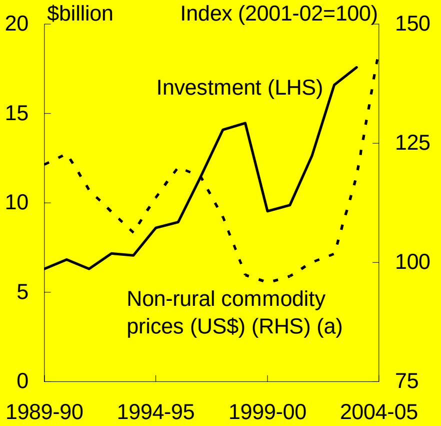


Source: ABS Cat. No. 5206.0 and Treasury.

Box 2: Mining capacity constraints

Global demand for commodities has increased more than expected over recent years, while resource production has increased only modestly. As a result, commodity prices have increased dramatically.

Chart A: Commodity prices and Australian mining investment

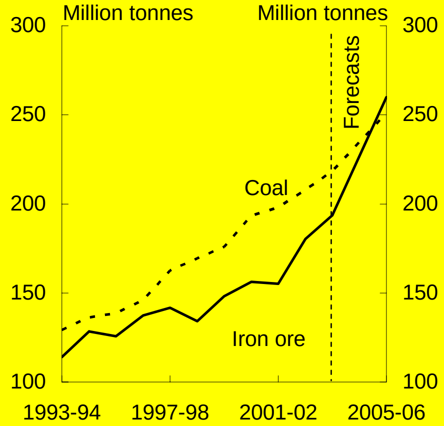


(a) Data for 2004-05 are year-average to April.
Source: ABS Cat. No. 5204.0 and RBA (original data).

The limited initial supply response reflects the large fixed costs inherent in mining projects. These costs mean that mining operations and supply chains are most profitable when operating close to capacity. Hence, there is often little spare capacity to meet an unexpected increase in demand.

Australian mining investment has surged following the increase in commodity prices since 2000 (Chart A). The resulting increase in output has already begun to lift export volumes (Chart B). There is still further productive capacity to come on stream, with resource exports expected to increase by a further 15 per cent by June 2006.

Chart B: Iron ore and coal export volumes



Source: Unpublished ABS data and Treasury (original data).

Some infrastructure constraints emerged as mining output increased. In vertically-integrated production and transport chains, such as in the iron ore and liquefied natural gas industries, these constraints are being addressed in tandem with increases in output. In cases where ownership of the production and transport chain is more fragmented, such as in the coal industry, infrastructure investment has tended to lag increases in production, leading to some bottlenecks.

Strong global demand and sustained high prices will encourage an increased supply of resources from Australia and the rest of the world. The interplay between rising global demand and supply makes predicting the future course of commodity prices particularly difficult. However, the mining sector is likely to be a significant contributor to national income in coming years.

The additional production flowing from new investment in parts of the mining sector has so far been outweighed by falling production for other commodities. Production in some of Australia's mature oil fields off Western Australia and in Bass Strait, for example, has fallen sharply over the past two years. This situation is expected to be redressed to some degree in 2005-06 as a significant expansion of capacity in areas such as liquefied natural gas and iron ore is brought into production.

After growing strongly in the late 1990s, export volumes for rural goods have not grown over the first half of this decade. The 2002-03 drought had a major impact on rural production. Grain production recovered strongly in 2003, but fell slightly in 2004. The production of livestock and some water-intensive crops has still not fully recovered from the drought. On the assumption of average seasonal conditions, rural exports are forecast to grow modestly in 2005-06.

Manufactured exports have grown more strongly, on average, than commodity exports in recent years. However, manufactured export growth has still been considerably below the average rate recorded through the 1990s. The maturing of some of Australia's manufactured export industries and the upward movement in the exchange rate since late 2001 explain some of this slowdown. The increasing quality and diversity of the goods produced by some newly industrialising countries, such as China, is also leading to increased competition and significant movements in the prices of some internationally-traded manufactured goods. It is difficult to predict precisely how Australia's exporters of manufactured goods will respond to these challenges, but a modest strengthening in manufactured export growth is expected in 2005-06.

Service exports have been broadly flat in recent years, partly reflecting the impact of a rising exchange rate and health and security concerns for international travel. Growth in service exports is expected to strengthen in 2005-06 in response to favourable world economic conditions.

Growth in imports is forecast to be 8 per cent in 2005-06, marginally slower than in 2004-05. Falling import prices and strong growth in all of the components of gross national expenditure have supported import growth in recent years. Slower growth in gross national expenditure over the forecast period will contribute to slower import growth.

The terms of trade

The terms of trade are expected to increase substantially in 2005-06, largely reflecting the convergence of strong world demand for commodities and relatively low growth in commodity supply. The exchange rate is broadly unchanged from the start of 2004, so the recent prices received for commodities in Australian dollars have generally tracked the price movements on world markets (usually expressed in US dollars). Continuing falls in import prices are also expected to support growth in the terms of trade.

In 2005-06, the terms of trade are forecast to increase by 12¼ per cent, after growth of 7.0 per cent in 2003-04 and expected growth of 9¾ per cent in 2004-05. This exceptional period of growth will take Australia's terms of trade to their highest level in 50 years.

In the late 1990s, the world supply of commodities grew strongly. Uncertainty around world economic developments, particularly following the Asian financial crisis in 1997, saw commodity prices fall to their lowest level in more than two decades in US dollar terms. This led commodity producers to reduce their investment in new capacity, notwithstanding the structural increase in global demand associated with the rapid growth in China and elsewhere. The sentiment of the time was reflected in the very strong interest in 'new economy' industries at the expense of 'old economy' industries such as mining.

Demand for commodities was relatively subdued in the following years, with most of the world's economies entering a period of subdued growth in 2001 and 2002. But some economies, most notably that of China, continued to grow strongly and increase their demand for commodities throughout these years. As the United States and, to a lesser extent, the rest of the world entered a period of stronger economic growth in 2003 and 2004, the demand for commodities quickly outstripped supply. As a result, commodity prices began to increase sharply.

Australia has benefited from these strong increases in world commodity prices and this is evident in the higher terms of trade. The prices for coal and iron ore, in particular, have increased substantially in recent rounds of contract negotiations with Japanese and Chinese buyers (see Box 3).

It seems unlikely that world commodity prices will be sustained at these levels indefinitely because the present high prices substantially exceed the cost of new production. Consequently, a large amount of investment in mining projects is already underway around the world, including in Australia. Continuing high commodity prices will encourage more investment. While the planning and construction lead times on mining projects are typically very long, meaning that supply responses typically lag demand changes, it is likely that the world supply of commodities will increase in 2005-06 and future years. For example, over the next three years, world production of iron ore is expected to increase by around 20 per cent.

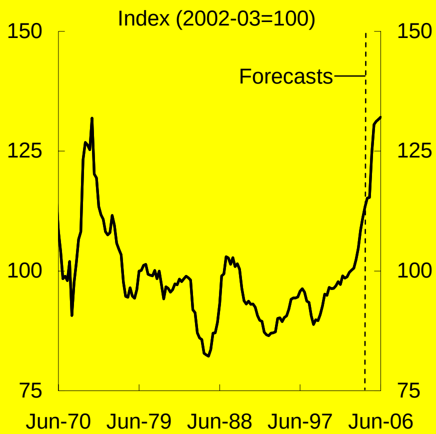
An increasing world supply of commodities should place downward pressure on commodity prices over time. The timing and extent of any such price adjustment is very difficult to predict. Since contract prices are typically struck before the beginning of the Japanese financial year on 1 April, any substantial adjustment is unlikely to occur before the June quarter 2006. However, there is a risk that Australia's terms of trade will fall over the medium term from their historical highs in 2005-06. This, in turn, carries significant implications for the budget projections for 2006-07 and beyond, particularly with respect to company tax collections from the mining sector. See Box 7 for a discussion of commodity prices and the budget projections.

Box 3: Booming commodity prices

Recent contract negotiations have locked in strong US dollar price increases in 2005 for some of Australia's key bulk commodity exports. In particular, hard coking coal prices are up by 120 per cent, iron ore prices are up by 70 per cent and steaming coal prices are up by 20 per cent.

Largely because of these export price increases, the terms of trade are expected to increase by 12¼ per cent in 2005-06, to be at their highest level in 50 years (Chart A).

Chart A: Terms of trade



Source: ABS Cat. No. 5302.0 and Treasury.

Assuming no change in the exchange rate, these commodity price increases will add approximately 2 per cent to nominal GDP in 2005-06. This additional income will benefit a number of sectors in the economy.

Mining companies will receive higher revenue, boosting their profits. Mining company shareholders (including superannuation funds) will also benefit, either from higher dividend payments or, if companies retain their earnings, stronger capital gains.

Higher prices, if sustained, will also support higher capacity utilisation and stronger investment in the mining industry with the effect of boosting production and exports. As a result, suppliers of goods and services to the mining industry will also benefit from stronger earnings. Although the mining sector is not labour intensive, employment may also increase modestly.

Governments will also benefit from higher royalties and company taxation.

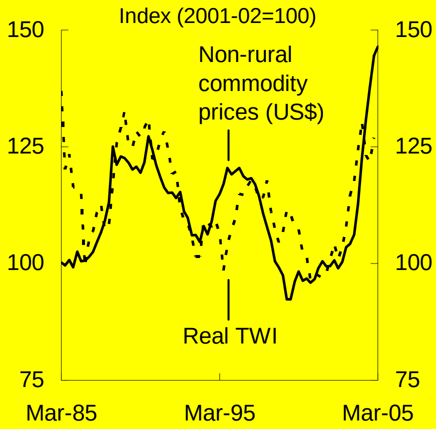
Higher commodity prices are expected to reduce the trade deficit by around 2 per cent of GDP. However, foreign investors in the Australian mining sector will receive some of the income generated by the higher commodity prices. Higher dividend payments and repatriated earnings of foreign investors are expected to widen the net income deficit component of the current account by around 1 per cent of GDP.

Thus, the increase in the net income deficit will partially offset the reduction in the trade deficit, with the overall current account deficit reduced by around 1 per cent of GDP.

Box 3: Booming commodity prices (continued)

This analysis is based on the technical assumption of an unchanged exchange rate. However, since the float of the Australian dollar in 1983, an appreciation of the exchange rate has generally accompanied an increase in world commodity prices (Chart B).

Chart B: Commodity prices and the real exchange rate



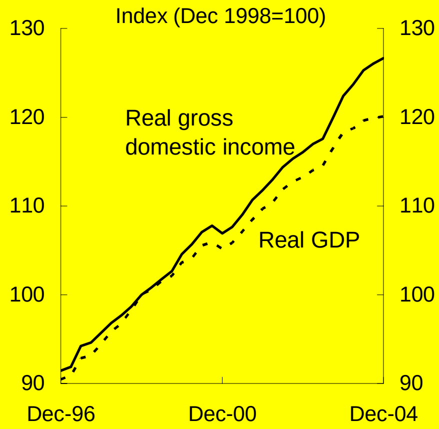
Source: RBA (original data).

If the exchange rate was to appreciate further in response to higher commodity prices, the benefits of stronger world demand for Australian exports would pass through the economy in a different way. The terms of trade and real incomes would still be higher. But, for resource exporters, the higher exchange rate would dampen the effect of the price increase on revenue. And for exporters of manufactures and services, and import-competing industries, a higher exchange rate would make it more difficult to compete.

Consumers and domestic producers would still benefit directly from improved purchasing power as import prices fall.

The increase in purchasing power is captured in the real gross domestic income (GDI) measure (Chart C). Real GDI is estimated as the volume of GDP plus the terms of trade effect.

Chart C: Terms of trade effect on purchasing power



Source: ABS Cat. No. 5206.0.

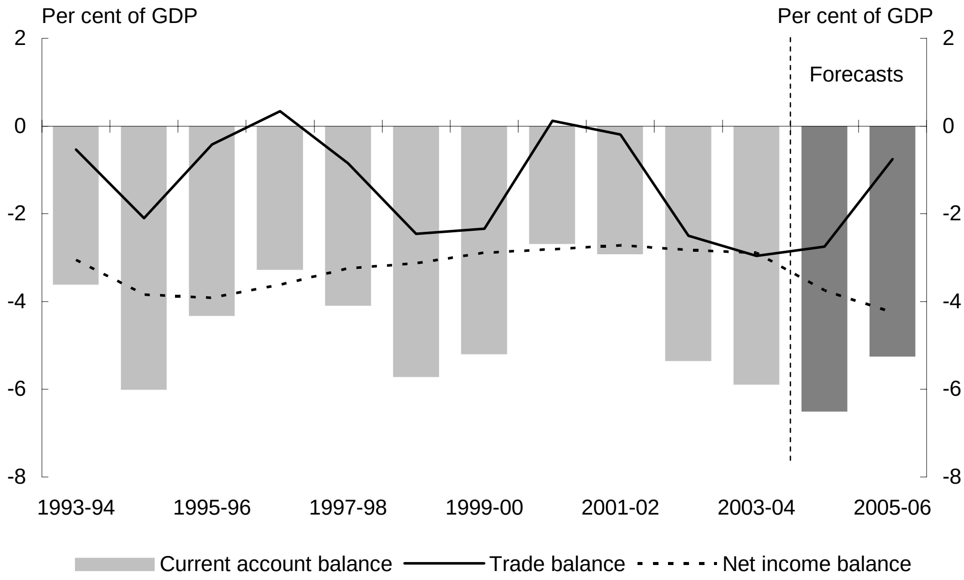
Regardless of how the benefits flow through the economy, the current high demand for Australia's commodity exports is generating considerable real income gains.

The current account

The current account deficit (CAD) has remained relatively high as a proportion of GDP in recent years, largely reflecting an increase in the trade deficit since 2001-02 (see Chart 8). As discussed in the net export section, export growth has been subdued in recent years, while import growth has remained robust, in line with strong growth in gross national expenditure. Australia's CAD is financed by an offsetting capital account surplus, the components of which are examined in Box 4.

An important influence on movements in the CAD over the forecast period will be the boom in commodity export prices. The net income deficit will increase as higher export prices result in higher profits being paid to foreign investors in the Australian mining sector, but this will be offset by the positive impact of higher prices on the trade deficit.

Chart 8: Current account balance



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

The CAD is forecast to narrow to 5¼ per cent of GDP in 2005-06 from an expected 6½ per cent of GDP in 2004-05. Higher commodity prices will contribute to this improvement in the CAD (see Box 3).

Box 4: The balance of payments and net lending

The balance of payments consists of the current account (goods, services and income transactions between Australia and the rest of the world) and the capital account (flows of funds between Australia and the rest of the world that are required to finance current account transactions).

A country that invests more than it saves records a current account deficit (CAD). This is financed by an inflow of funds from the rest of the world, which is recorded as a capital account surplus.

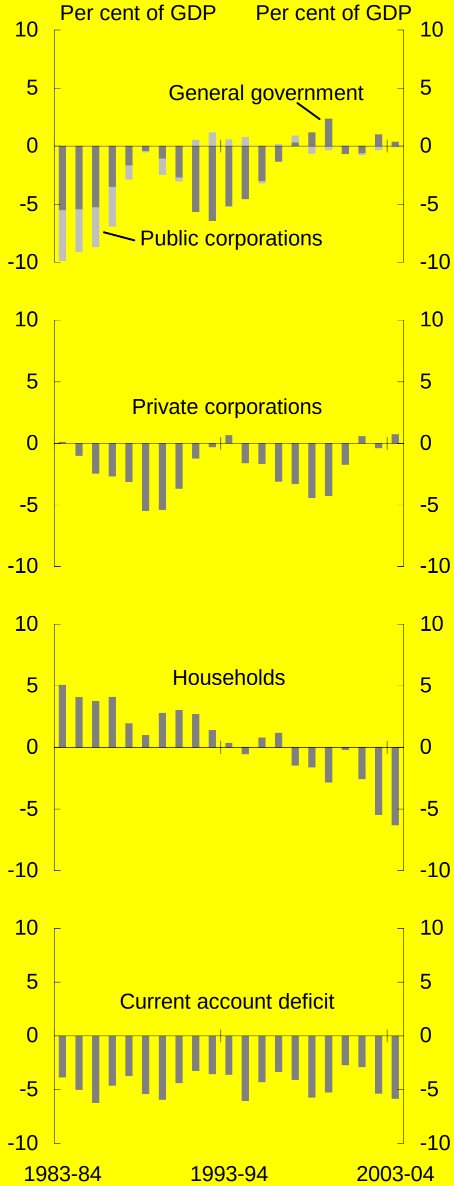
The net lending framework decomposes the economy's financing requirements between the household, corporate and public sectors. The net lending framework for Australia is presented in Chart A. Negative figures indicate a requirement to borrow from other sectors or from the rest of the world.

Since 1996-97, the government sector has become a small net lender on average, making a positive direct contribution to the current account balance.

Private corporations have also become small net lenders in recent years, as companies have funded investment from profits rather than borrowings.

Almost all of the recent increase in the CAD is attributable to the household sector. In other words, households have been borrowing from other sectors and, ultimately, from the rest of the world, via the banking system.

Chart A: Net Lending



Source: ABS Cat. No. 5204.0, 5302.0 and Treasury (original data).

Box 4: The balance of payments and net lending (continued)

The increase in households' net borrowing is partly a result of higher household wealth (from higher house prices), leading households to invest more and save less.

Higher investment and lower saving is also a response to a more stable and resilient economy with sustained employment growth and low inflation. In a stable economy, households may choose to hold a lower level of precautionary savings than in a volatile economy.

In addition, deregulation of financial markets, combined with low inflation, has lowered borrowing costs. This has allowed households greater flexibility to spread their consumption and investment decisions over time.

The outlook for 2005-06 is for GDP growth to rebalance away from domestic to external sources. Accordingly, while the corporate and government sectors are expected to remain net lenders, the household sector's net borrowing is expected to decrease in line with easing dwelling investment and consumption.

Labour market, wages and prices

Labour market

Employment has continued to grow rapidly through 2004-05, with the unemployment rate falling to a 28-year low of 5.1 per cent in December 2004. Construction employment has increased strongly over the past year, reflecting the high levels of economic activity in that sector.

Forward indicators of employment, such as measures of job vacancies, point to further solid employment growth in coming months. For example, the Australian Bureau of Statistics' job vacancy series increased by around 40 per cent through the year to February 2005.

Employment growth is expected to moderate to 1¾ per cent in 2005-06 as the effects of recent slower GDP growth feed through to the labour market. In particular, employment growth in the construction sector is expected to slow, reflecting the flattening of growth in residential and commercial construction.

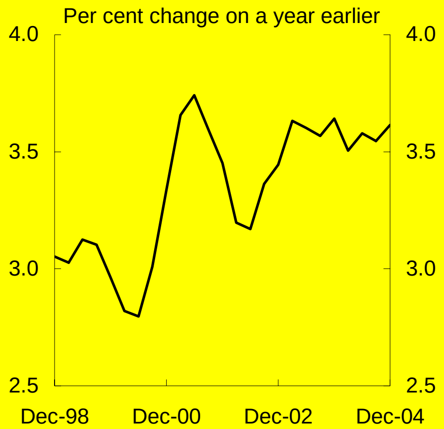
The unemployment rate is forecast to remain near 5 per cent through 2005-06 after averaging around 5¼ per cent in 2004-05. Workforce participation is forecast to remain high by historical standards at 63¾ per cent on average in 2005-06. This is a little below its level of recent months. This Budget contains measures to increase workforce participation over the medium term. In the short term these measures will place upwards pressure on measured unemployment as new entrants to the labour market take time to find jobs.

Box 5: Labour market flexibility

The labour market has performed very strongly over the past 12 months, with the unemployment rate falling to a 28-year low.

Given this historically low outcome, it is not surprising that some business surveys are indicating that suitable labour is becoming more difficult to find. However, there is currently no evidence of widespread labour shortages or generalised wage pressure (Chart A).

Chart A: Wage price index



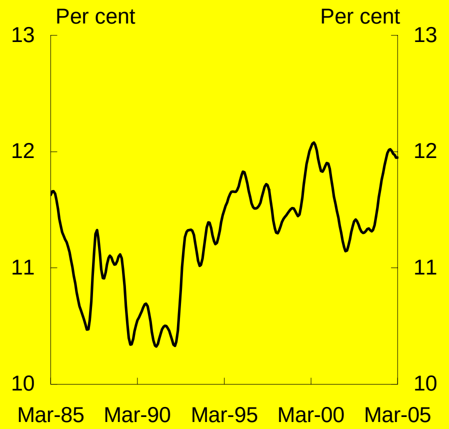
Source: ABS Cat. No. 6345.0.

This combination of low unemployment and moderate wage growth reflects past labour market reforms which have created more flexible working arrangements. This has led to a more efficient allocation of labour, higher productivity and increased real wages without triggering inflationary pressure.

These reforms have also encouraged more people to participate in the labour force, with greater flexibility in the degree to which they participate. For example, part-time employment now accounts for around 28 per cent of total employment.

Given the right circumstances, around a quarter of these workers have indicated they would like to work more hours, increasing the available pool of labour. Employers have been drawing on this pool, with the flows of workers from part-time to full-time employment around record highs (Chart B).

Chart B: Proportion of part-time workers gaining full-time employment



Source: ABS Cat. No. 6203.0, 6291.0.55.001 (trend data).

The ability to utilise existing workers more effectively should lessen the impact of tighter labour market conditions on economic activity and inflation.

While the unemployment rate is at a 28-year low, there is further scope to increase labour inputs to production through the better use of under-utilised labour and by encouraging greater workforce participation (see Box 5).

Wages

Moderate wage growth in recent years has provided a good foundation for sustained economic growth. The Wage Price Index has averaged growth of around 3½ per cent for the past two years. These moderate outcomes are welcome in the light of a steadily falling unemployment rate.

Reforms in recent years to boost the economy's productive potential, particularly those in the area of workplace relations, have supported this healthy combination of strong employment and moderate nominal wage growth (see Box 5). Statement 4 in the 2004-05 Budget discussed labour market flexibility issues in more detail.

Wage growth is expected to increase over 2005-06, with the Wage Price Index forecast to grow by 4 per cent. Some localised wage pressure has appeared in specific industries and occupations, particularly in those areas affected by conditions in the mining sector. With the unemployment rate at a 28-year low, it is likely that some localised wage pressures will remain. Such relative wage adjustment is an important signalling mechanism in a high employment economy, helping to direct workers to the areas of their highest productive value.

At this stage, there is no evidence of more generalised wage pressure, and the expected more modest employment growth in the period ahead should help to contain overall wage pressure. However, it will remain important that wage growth is backed by increases in productivity on average — particularly with the current very low levels of unemployment — to support further sustainable economic growth.

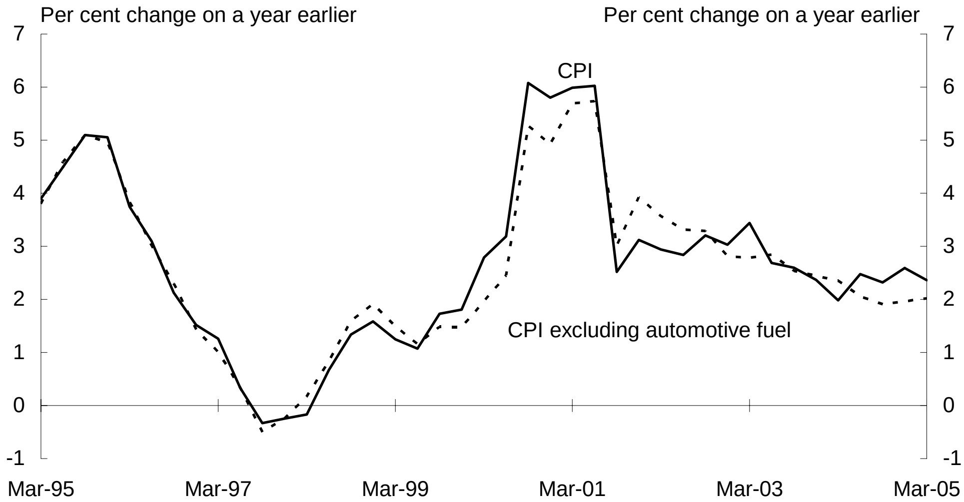
Prices

Inflation has been contained in recent years (see Chart 9), reflecting moderate growth in unit labour costs, the effects of a higher exchange rate and vigorous competition in the retail sector. The Consumer Price Index (CPI) increased by 2.4 per cent through the year to the March quarter 2005. Although petrol prices are expected to place some further upward pressure on consumer prices in the near term, inflation is expected to remain moderate, with the CPI forecast to grow by 2½ per cent through the year to the June quarter 2006.

Unit labour costs are forecast to increase in 2004-05, reflecting a cyclical slowing in productivity growth and a slight increase in wage growth. While this will put some upward pressure on inflation, businesses are expected to look through some of the cyclical slowing in productivity growth in order to ameliorate volatility in retail prices.

Oil prices have continued to exert some upward pressure on the CPI in recent quarters. The direct impact of oil prices has been through higher petrol prices, although the prices of some other goods and services — air fares for example — have also been affected. Oil prices are assumed to remain broadly unchanged over 2005-06 and, therefore, petrol prices are expected to stabilise.

Chart 9: Inflation



Source: ABS Cat. No. 6401.0 (original data).

Box 6: Real GDP projections

The economic outlook includes projections for real GDP growth beyond the immediate two forecast years. From the 2005-06 Budget, this assumption is amended from 3½ per cent to 3¼ per cent per annum for 2008-09 and beyond.

The Intergenerational Report (IGR) notes that falling labour market participation due to an ageing population is expected to lower potential GDP growth in the coming decades.

Projections of GDP growth for 2008-09 will begin to reflect the IGR projections of declining participation rates and hence employment growth. Specifically, projections for employment growth have been adjusted down to 1¼ per cent in 2008-09, bringing projected GDP growth down to 3¼ per cent (Table A).

Table A: Economic projections(a)

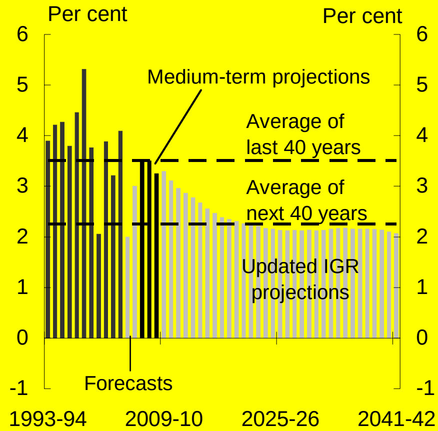
	2006-07	2007-08	2008-09
Employment(b)	1 1/2	1 1/2	1 1/4
Productivity	2	2	2
Real GDP	3 1/2	3 1/2	3 1/4
Wages(c)	3 3/4	3 3/4	4
CPI	2 1/2	2 1/2	2 1/2

(a) Percentage change on previous year.
(b) Labour Force Survey.
(c) Wage Price Index.
Source: Treasury.

The projections for 2006-07 and 2007-08 assume that the wage share of GDP continues to fall. From 2008-09, compensation of employees and corporate profits are assumed to grow at the same rate as nominal GDP, keeping the wage share constant. As a result, wages are projected to grow by 4 per cent in 2008-09.

The long run implications for GDP growth of adopting the IGR projections for declining aggregate participation and hence employment growth are shown in Chart A.

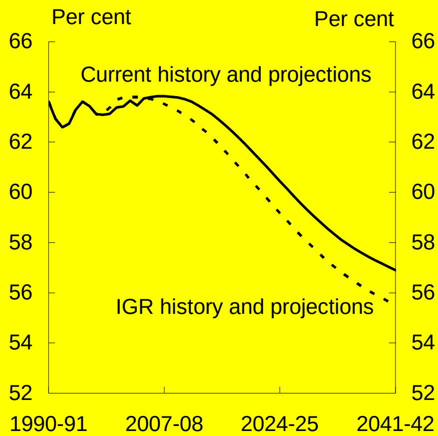
Chart A: Real GDP growth



Source: ABS Cat. No. 5206.0 and Treasury.

These projections are based on new population and participation data available since the 2002-03 IGR. With these new data, the peak in participation is now projected to occur in 2006-07 (Chart B).

Chart B: Participation rate



Source: ABS Cat. No. 6202.0 and Treasury (original data).

Box 7: Nominal GDP projections

Nominal GDP is forecast to grow by 7½ per cent in 2005-06, largely reflecting increases in Australia's commodity export prices.

Nominal GDP has grown very strongly for a number of years. In 2003-04, nominal GDP grew by 7.3 per cent, largely reflecting the impact of housing demand on both real GDP and domestic prices. Strong growth in the terms of trade and the effects of higher oil prices are expected to result in nominal GDP growth of 6 per cent in 2004-05.

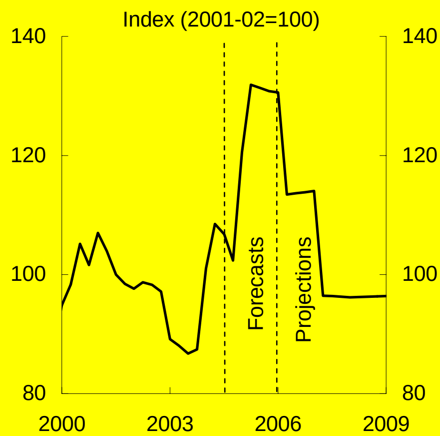
Nominal GDP projections, for the period 2006-07 to 2008-09, are typically based on underlying trends for real GDP and the GDP deflator – they are not forecasts. However, if the GDP deflator is projected at its historically-based trend growth rate, it would imply that commodity prices would remain at historically high levels over the entire projection period.

Beyond the forecast period, world supply for commodities that Australia exports is expected to increase in response to the recent surge in demand. This is likely to place downward pressure on Australia's export prices. As a result, not all of the recent boost to Australia's nominal income will be permanent.

How much of recent nominal income gains will be unwound in the projection period is a matter for judgement.

The approach, adopted in this Budget's fiscal projections, is to assume that commodity prices return to their long-run average level over the first two years of the projection period (Chart A). As a result, nominal GDP growth in 2006-07 and 2007-08 is not projected to grow as strongly. Projected real GDP growth is unaffected by the technical assumption for commodity prices.

Chart A: Commodity prices



Source: ABS Cat. No. 5302.0 and Treasury.

The interplay between rising global demand and supply makes predicting the future course of resource prices particularly difficult. Therefore, there is considerable uncertainty around the technical assumption for commodity prices.

STATEMENT 4: PROSPERITY AND SUSTAINABILITY

Australia's successful economic performance over the last decade provides a sound basis for future national prosperity if the right decisions are made for the future. Importantly, that performance also provides valuable experience to help us determine what policy measures need to be implemented to expand opportunities for all Australians.

Over the next 40 years the number of people over the age of 65 is projected to double. However the number of people of traditional working age will hardly increase. This presents a challenge to the sustainability of economic growth. The demand for greater availability and higher quality aged care, and the rising cost of health care — only partly due to population ageing — will put pressure also on fiscal sustainability. Those concerns and others, such as maintaining the environment, will become more pressing over time. Solutions will require longer planning horizons than have been employed in the past.

Policy choices will have little effect on the numbers of people of traditional working age. Solutions will therefore need to focus on facilitating further productivity improvements and increasing labour force participation for those of working age. This will involve some difficult tradeoffs.

The task will be made easier if there is widespread understanding of policy drivers and an environment where firms and individuals are able to respond positively to the opportunities that sound policy can create.

Contents

STATEMENT 4: PROSPERITY AND SUSTAINABILITY

This statement examines the evolution in policies and institutions most likely to contribute to further increases in Australia's prosperity and the wellbeing of all Australians over the medium to long term. Those same policies and institutions are also those most likely to enhance Australia's ability to deal with future economic shocks. While further policy evolution will not be easy, the cost of failing to do so would be significant.

Australia's very successful recent economic performance provides valuable insights into the types of decisions needed to enhance opportunity for all Australians, while providing a solid foundation for continued national prosperity.

Our continued prosperity relies on making better use of our natural, man-made and human resources. This is not a simple task and necessarily involves some difficult tradeoffs. Subjecting policies to the following tests will inform decision-making.

- Do they improve prospects of sustaining and improving the quality of our natural, man-made and human resources?

- Do they improve the prospects of public and private resources being used more productively?

- Do they promote participation in the paid and voluntary workforce?

- Do they make the economy more resilient and adaptable to possible shocks and challenges?

- Are they cost effective and sustainable in the long term, irrespective of whether their objective is achieved through taxation, expenditure or regulation?

MAINTAINING A STRONG ECONOMY

Over the past decade Australia has performed very well against the measures of income, wealth, human development and employment. This strong performance is based on a set of sound policies, institutions and investments that have enabled Australia to make better use of its resources.

The strength of the economic performance, and the Australian Government's sound fiscal position, present a unique opportunity to implement a cohesive policy agenda that will underpin strong economic growth now and over the decades to come.

Just as the decisions of the past have created our prospects today, so too, the decisions made today and into the future will influence our long term prosperity and opportunity.

Those decisions will be taken against the background of population ageing, rising health and aged care costs, and threats to the quality of the natural environment that will challenge the sustainability of our recent impressive performance. Policy improvements implemented now can help to soften the downside risks of the future.

Realistic changes to rates of fertility and immigration would have little discernible impact on the rate at which the population is projected to age over the next half century. Therefore maintaining the per capita growth rates to which Australia has become accustomed will require ongoing improvements in productivity growth and labour force participation.

Strong, sustainable economic growth is needed to generate the public and private wealth to meet growing demands, not only to support the growing proportion of elderly people in the community, but also to fund increased expenditure on health care which will be driven not just by ageing but by technological improvements as well. Without strong, sustainable economic growth Australia would eventually be forced to adopt new or higher taxes to meet recurrent demands. High taxes and debt repayments would, in turn, act as a drag on economic growth.

The discussion in **Building on a strong foundation** focuses on the public and private decisions, and other domestic and international factors, that have produced the strong economic performance of the past decade or so. Policy has focused on improving the efficiency of the private sector and establishing a stable medium-term macroeconomic framework through a series of coordinated and complementary reforms. In combination, those policies have helped Australians benefit from favourable domestic and international influences and overcome adverse economic shocks such as global slowdowns.

The subsequent sections examine those policy reforms that, in light of the ageing population, are most likely to contribute to increased future prosperity. Such reforms could underpin productivity growth and increase levels of participation in both the paid and voluntary workforce.

As **Being more productive** discusses, that will require:

- further and ongoing improvement to infrastructure investment decisions;
- increasing competition through continued reform of domestic labour and product markets and enhanced international engagement;
- improving the cost-effectiveness of government;

- avoiding unnecessary regulatory complexity; and
- taking better account of costs and benefits in decision-making, particularly in making sound decisions on the use and maintenance of the natural environment.

With the ageing of the population it will be important that more Australians be given the opportunity of **Improving participation and sharing Australia's prosperity** through policies that support participation in the labour force and society more generally. They include strengthening the capacity to participate through improved education and health, improving the balance of incentives to shift from welfare-to-work to avoid cycles of dependency, and enhancing the flexibility of working arrangements. Decisions to participate in paid or unpaid employment, and tradeoffs between work and leisure, are inherently personal ones. However, government policies can and do influence those choices.

Australia does not face the public debt problems of many countries. However, we will face stark choices in the future if we do not act pre-emptively to address emerging fiscal pressures from an ageing population. This requires **Maintaining a disciplined approach to fiscal policy**, including new strategies that take a broader view of the Australian Government's balance sheet and address future pressures on the tax base.

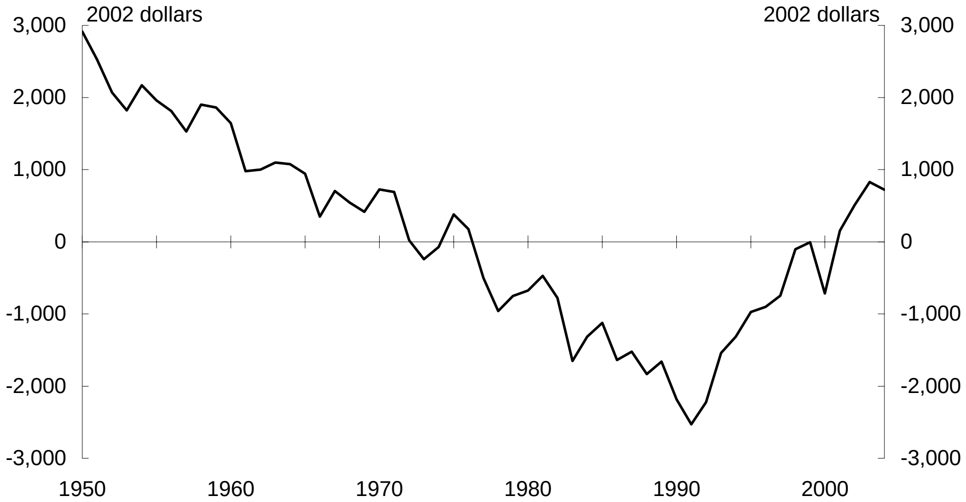
BUILDING ON A STRONG FOUNDATION

Australia's recent economic performance is impressive, both compared with other developed countries and by historical standards. In the four decades from 1950, growth in GDP per person — one indicator of improvements in living standards — usually fell below the OECD average rate of growth. However, in the past decade or so Australia's performance has improved dramatically (Chart 1). GDP per person has grown much faster, on average, than in both the United States and the OECD, raising Australia from 18th highest GDP per person among OECD countries to 8th today.

This section highlights the main drivers of Australia's new prosperity and discusses the ways in which Australians have benefited.

Chart 1: Australia's economic revival

The difference between Australian and OECD average GDP per person[(a)]



(a) OECD data are for the 24 longest standing OECD member countries.
Source: Groningen Growth and Development Centre and The Conference Board (2005).

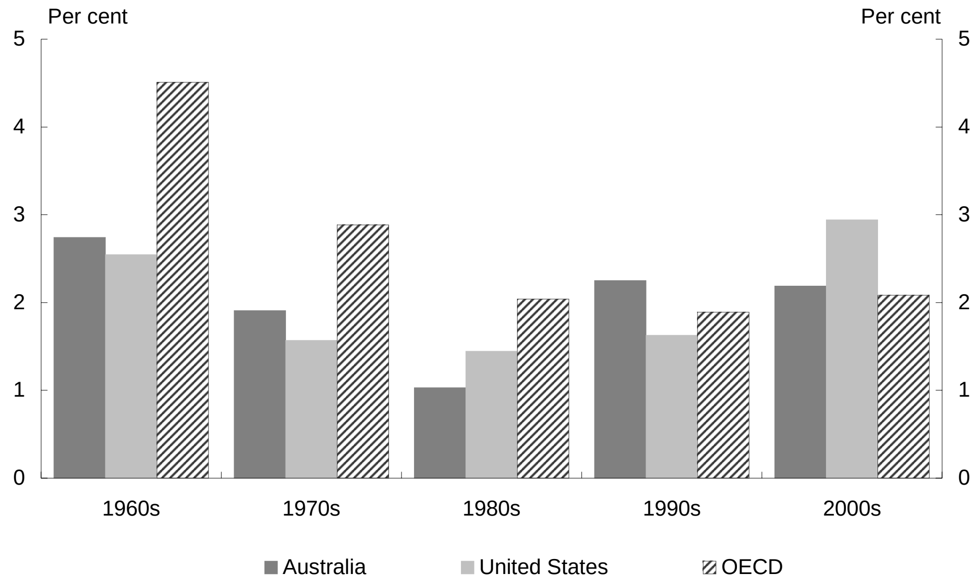
The reasons for Australia's prosperity

One approach to understanding the drivers of economic growth is to consider trends in population growth, labour force participation and productivity (see the detailed discussion in Budget Paper No. 1, *Budget Strategy and Outlook 2003-04,* Statement 4). Improvement in living standards, as measured by GDP per person, is the result of growth over time in the proportion of the population that is of working age, the number of hours worked by each person of working age, and the volume and quality of goods and services produced during those hours of work.

From the early 1990s, higher rates of labour productivity growth, rather than more favourable changes in the population age structure, or labour force participation rates, have driven Australia's strong economic performance. Labour force participation, as measured by the combination of average hours worked and the rate of employment among those aged 15 years and older, contributed little to growth in output and average incomes over the last four decades. While the increase in the participation of women in the workforce has more than offset the gradual decline in the participation of men, increased aggregate participation has been largely offset by the decline in average hours worked, largely reflecting the increase in part-time work (ABS 2005f; Reserve Bank of Australia 1997).

Beginning at the start of the 1990s, Australia's rate of labour productivity growth revived following decades of lagging other major developed countries. Productivity grew more rapidly during the latter half of the 1990s than during any comparable period in the past forty years. Australian labour productivity even grew faster than the 'new economy' of the United States (Chart 2). The revival since the 1990s is especially remarkable in that it did not accompany a worldwide productivity boom. Indeed the average rate of labour productivity growth was slower across the OECD during the 1990s than in the previous decade. This suggests that additional circumstances unique to the Australian economy were responsible.

Chart 2: Labour productivity growth(a)



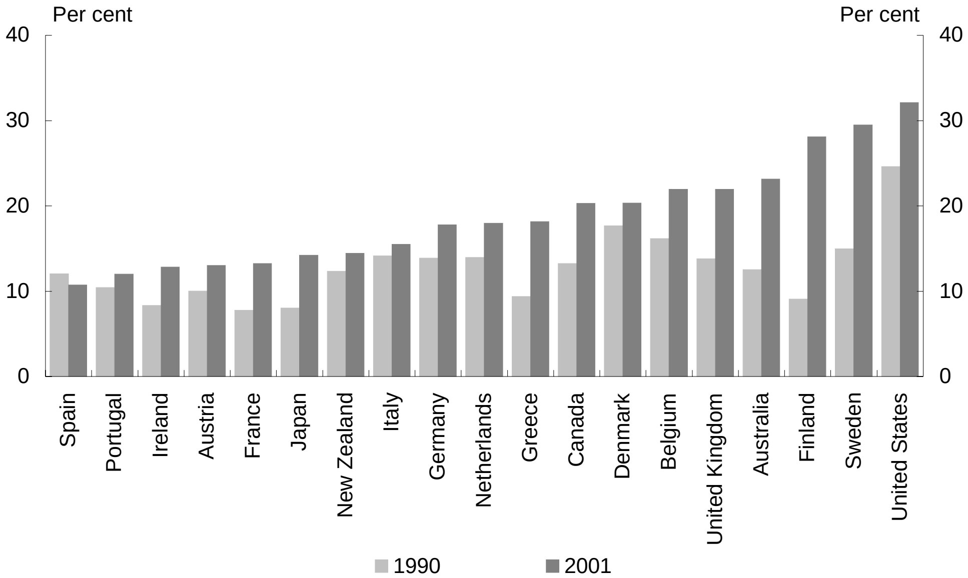
(a) OECD data are for the 24 longest standing OECD member countries. Data are average annual growth rates.
Source: Groningen Growth and Development Centre and The Conference Board (2005).

Labour productivity growth over time reflects:

- increases in capital per worker (that is, capital deepening);
- improvements in labour quality through education and experience; and
- improvements in the efficiency with which labour and capital are used, through innovative work practices, the achievement of economies of scale and technological developments.

In the 1990s, the rate of capital deepening accelerated from the slow pace of the 1980s (ABS 2004a). The rapid investment in, and use of, information and communication technology was particularly important. Australia has been among the world's leading users of information and communication technology (Chart 3).

Chart 3: Investment in information and communication technology
Share of non-residential fixed capital formation



Source: OECD (2005b).

However, improved efficiency (often referred to as multi-factor productivity) was the predominant driver of Australia's productivity revival (ABS 2004a). Australia's multi-factor productivity growth during the 1990s was stronger than for all other OECD countries for which data are available, except Finland and Ireland (OECD 2005b).

Central among the drivers of this improved efficiency was the broad and deep programme of mutually reinforcing reforms implemented during recent decades (IMF 2004; OECD 2005a; Parham 2004). Key reforms included: liberalising trade, foreign investment, financial markets and workplace relations regimes; tax reform (including reforms of the indirect tax system and targeted incentives to work and save); corporate law reform; and implementing a broad-ranging National Competition Policy agenda.

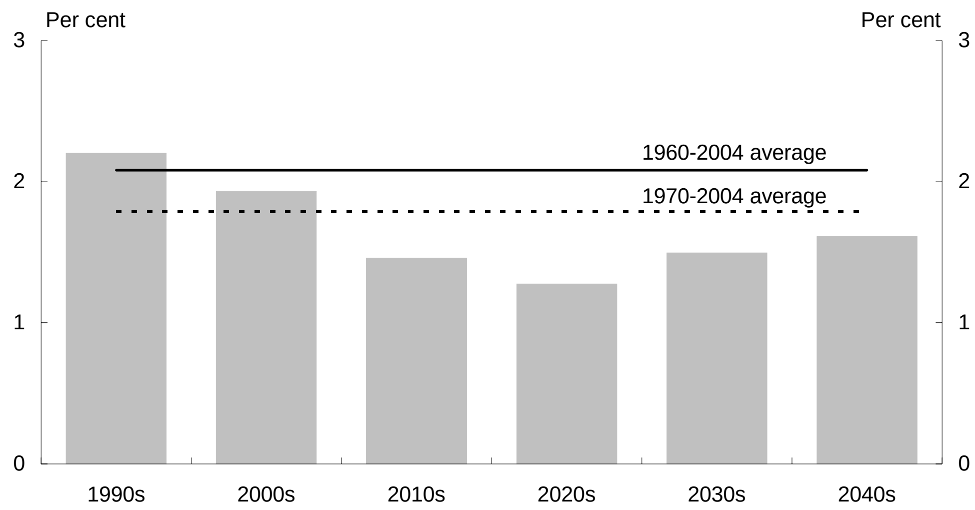
The resulting increase in domestic and international competition encouraged both a more efficient allocation of resources and a more vigorous pursuit of productivity improvement. More flexible labour markets permitted the reorganisation of work practices to take advantage of improvements in technology and skills. More flexible financial markets improved access for new, developing industries to the capital they required.

Microeconomic reforms and changes in behaviour have worked to raise the level of output the economy is capable of producing. They have been complemented by the Australian Government's macroeconomic reforms in the mid-1990s which placed both fiscal and monetary policies within sustainable medium-term frameworks. Sound and sustainable macroeconomic policies have delivered a smoother pace of economic growth. They have helped avoid inflationary pressures while accommodating a steady decline in the unemployment rate. The resulting stable, low interest rate environment has provided security for firms to innovate and invest.

In recent years, Australian incomes have been bolstered by favourable changes in the relative prices of our imports and exports. Rapid economic development in China and India raised global demand and prices for the resources that Australia exports, while reducing the world price for manufactured imports. This has continued previous trends that resulted from rapidly declining prices for information technology and communications equipment. Shifts in the terms of trade will influence the direction in which Australia's manufacturing, mining and service sectors develop and contribute to ongoing prosperity.

The challenge will be to continue to improve living standards as the baby-boomer generation moves into retirement and causes a decline in the proportion of the population of traditional working age (15 to 64 years, that is, between compulsory school and age pension age). This will tend to reduce the proportion of Australians participating in the labour force and slow economic growth (Chart 4).

Chart 4: Projections of average annual growth in GDP per person



Source: ABS (2004a); and Productivity Commission (2005a).

The benefits of increased prosperity

The benefits of Australia's greater prosperity have been widely shared.

More Australians are now able to find work, with more than 1.5 million jobs created since 1996 (ABS 2005g). This has permitted a record high proportion of people of traditional working age to be engaged actively in the workforce. The unemployment rate has fallen from a peak of almost 11 per cent in 1992 to around 5 per cent, the lowest rate since the mid-1970s.

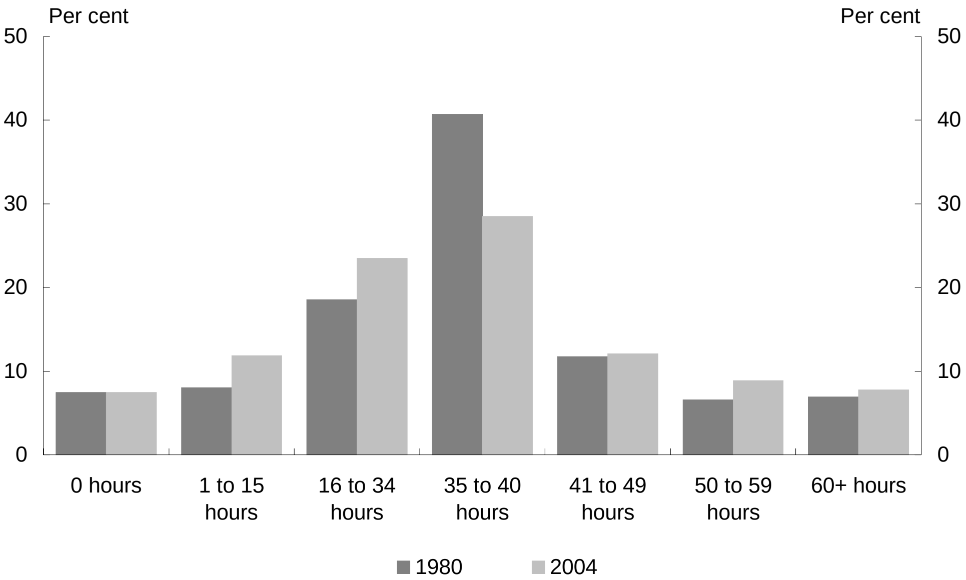
The disposable incomes of Australian households have increased. Strong productivity growth has allowed real wage rates to increase. On average, adults working in full-time jobs earned around $200 more per week in 2004 than they did in 1990 in 2004 dollars (ABS 2005b, 2005c). The benefits of real wage growth have been shared with Australians on a wide range of pensions, including the Age Pension, as those pensions increase in line with male total average weekly earnings.

Australian households now also have greater flexibility to manage their work, study, personal and leisure time. This is illustrated by the broader distribution of working hours (Chart 5). Part-time and casual work enables people to tailor their work to the demands of personal commitments and enables employers to meet better the demands of their customers. Almost half of the jobs created in the past decade have been part-time (ABS 2005a). While the majority of part-time workers are satisfied with the number of hours they work, a minority would prefer to work more hours.

This flexibility has allowed more Australians to study beyond the compulsory school age while managing work commitments. Almost two-thirds of those enrolled in post-secondary education or training are participating in the labour force, with a majority working part-time (ABS 2004b).

Chart 5: Employment by hours worked per week

Per cent of employed persons



Source: ABS (2005f).

Australians also have more flexibility to choose the time at which they retire. Although Australians are living longer than a generation ago, many are retiring earlier from full-time work. Some have moved into more flexible work arrangements, while others are involved in caring and other voluntary roles, or simply enjoying more leisure. Others have chosen to continue to work beyond age pension age.

Economic growth also has strengthened Australian household balance sheets. Household wealth has doubled over the past decade (ABS 2004a). This has been assisted by increased coverage and rates of saving into superannuation over the past two decades. Reliable employment also has provided households with greater capacity to save, borrow and invest for their futures.

Economic prosperity has allowed the Australian Government to expand the provision of public services while lowering tax rates. In addition, sound fiscal management has contributed to a reduction in Australian Government debt levels to among the lowest in the OECD (OECD 2004b).

Australia’s economic development has also allowed the achievement of broader social objectives. The United Nations measures such achievements using a Human Development Index (United Nations 2004). It considers improvements in human capabilities and opportunities by incorporating indicators of health and education together with output per person. By this measure, the wellbeing of Australians ranked the third highest of 177 countries in 2002. This is 11 places higher than in 1990 and nine places higher than rankings based on output per person alone.

The challenge is to maintain and further improve the policy and institutional environment for future prosperity.

BEING MORE PRODUCTIVE

Productivity growth is central to determining future living standards. Productivity growth is about getting more out of the finite resources available — working smarter, not harder. Increased productivity will provide more and higher quality goods and services and greater choice for Australians.

Australia’s productivity growth will depend both on the development of technology throughout the world that expands the productivity potential for all countries and continued improvement in domestic performance that will see Australia move closer to the productivity potential inherent in world best practice.

There is good reason to be optimistic about future productivity growth. International productivity potential may continue to expand rapidly through ongoing improvements in technology, including information and communication technologies. Strong competition and increasing openness to international trade and investment will encourage Australian businesses to make best use of such developments. Such growth can be supported through appropriate infrastructure provision, sound governance arrangements in both the private and public sectors and efficient management of our natural resources.

Despite recent strong productivity growth, Australia remains well below international productivity potential. In aggregate, Australian workers produce only around 80 to 85 per cent as much per hour as their peers in the United States (Groningen Growth and Development Centre and The Conference Board 2005). While the aggregate data mask significant sectoral differences, it is clear that a range of policy reforms could help Australia close this gap further.

However, it needs to be recognised that a number of factors peculiar to Australia are likely to hinder the ability to close the gap entirely. Geography affects economic success. Australia's small and dispersed population limits our exploitation of economies of scale, reduces the intensity of competition and increases transport costs compared with larger and more concentrated markets (Box 1). Distance and population will inevitably constrain Australia in achieving world-leading productivity performance in at least some industries and, hence, in aggregate GDP per person. Nonetheless, significant improvements can still be made with the right policies and economic environment.

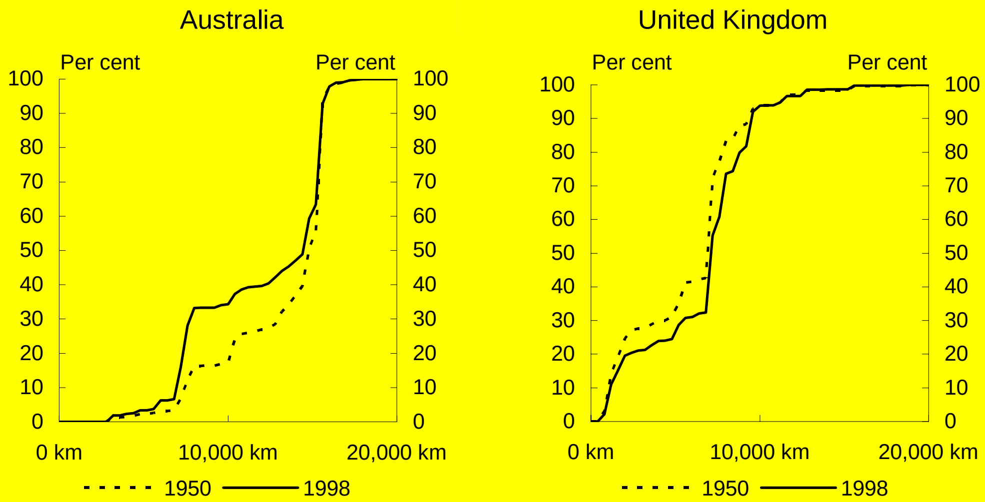
Box 1: Australia's economic remoteness

Australia has a small and dispersed population and is remote from the majority of the world's economic activity.

Australia has only 20 million people spread around the world's sixth largest land area. No two cities of more than one million are closer than 600 kilometres apart. In comparison, California has around 34 million people in a land area one-twentieth of Australia's (McLean and Taylor 2001).

Australia is second only to New Zealand in the OECD as the most remote economy from world economic activity. This is despite the recent rapid economic development in Asia. From the 1950s to the 1990s, the proportion of world GDP within 10,000 kilometres of Sydney increased from 17 per cent to 34 per cent (Chart 6). In comparison, 94 per cent of world GDP was within 10,000 kilometres of London in both the 1950s and the 1990s.

Chart 6: Distance to world GDP from Australia and the United Kingdom[(a)]



(a) Charts show the percentage of world GDP within certain distances of Sydney and London.
Source: Ewing and Battersby (2005).

Enhanced international integration and engagement

Higher productivity can be achieved by specialising in the industries to which Australia is best suited and by achieving economies of scale and scope. A small population and the costs of trading both within Australia and with major international markets constitute key economic hurdles to Australia achieving world-best levels of productivity (Box 1). Effective international integration can help reduce the limiting effects of Australia's geography and relatively small population.

Australia has taken significant steps to liberalise cross-border movement in goods and services, capital and people. This has resulted in:

- access to cheaper and better inputs and final goods and services;
- more efficient allocation of natural, man-made and human resources, with greater specialisation in areas of comparative advantage;
- access to international financial markets to fund investment, smooth consumption and expenditure over time, and share risks;
- transfer of skills and technology; and
- increased competition, promoting innovation and dynamic efficiency.

While increased global integration opens new opportunities for exchange, it also raises the need to manage new risks, including international economic and financial shocks, international crime, terrorism and contagious diseases.

As a small, open economy, Australia has a strong interest in the development of rules-based multilateral systems governing such areas as trade, investment, taxation, financial regulation, terrorist financing and money laundering. However, bilateral and regional integration is becoming increasingly important within East Asia. This region accounts for around half of Australia's trade (ABS 2005e) and its importance to the world economy has increased considerably over recent decades. The trend will continue as China and other emerging Asian economies continue to develop rapidly.

For Australia, the shift toward regionalism and bilateralism within Asia, most notably in trade policy, raises difficult questions about the appropriate balance between multilateral, regional and bilateral engagement. Nevertheless, a well-considered approach to regional and bilateral engagement can complement multilateral arrangements. When entering bilateral and regional agreements, it is important to focus on maximising potential gains and not adding unduly to the complexity of international trade and investment rules. The benefits of international trade and investment are best achieved when accompanied by reductions in behind-the-border barriers to new entrants, whether foreign or domestic.

Maintaining and investing in Australia's infrastructure

Infrastructure plays a key role in facilitating economic activities and contributing to Australia's general wellbeing. Both labour and capital rely upon access to efficient infrastructure to underpin their productivity. Over the past 20 years, Australian governments have implemented wide-ranging reforms to boost productivity in infrastructure sectors and contribute to economic growth. The recent Review of National Competition Policy Reforms (Productivity Commission 2005b) found that productivity gains in the six major infrastructure sectors that underwent most reform since 1990 permanently added 2.5 per cent to GDP. For example, output per worker in electricity, gas, urban water, telecommunications and rail freight more than doubled over the 1990s. Productivity gains have lowered prices and raised average incomes.

In the process of reform, governments have had to grapple with complex issues of ownership, regulation and contract arrangements, and to develop sound decision-making frameworks to encourage appropriate investment decisions. Despite significant progress, challenges remain in many areas.

Given its nature, infrastructure often requires some form of government involvement — this may be in the form of direct provision, planning and coordination of networks, or regulation of monopoly assets. Where government provision is necessary, effective investment decision-making should involve sound cost-benefit analysis.

Many governments here and abroad have privatised some infrastructure businesses, such as in the energy, transport and communications sectors, that generated sufficient revenue to be financially viable. In those cases, the focus for governments has shifted from that of ownership to facilitating vigorous competition or, where that is not possible, regulating prices charged by monopoly networks.

Some governments have retained ownership of assets in key sectors together with regulatory responsibility and political accountability. The conflict between those roles can put at risk effective pricing and investment decisions. Government intervention is still preventing prices from reflecting the true economic cost of production in some infrastructure service markets.

For example, some state governments in Australia are discouraging potential new private-sector investors by continuing to own electricity assets, cross-subsidising their generators and retailers, and capping retail prices (Productivity Commission 2005b). Few infrastructure facilities utilise time of day or congestion pricing for infrastructure services. Further, most rural and urban water prices currently do not take account of the value of water in alternative uses and water trading regimes are in their infancy.

Regulated price setting at the appropriate level is always a difficult process. Depending on how prices are set, suppliers may invest too much or too little in infrastructure. Either case can lead to inefficient use of scarce resources — reducing the resilience and reliability of networks and lowering overall productivity and economic growth. Moreover, infrastructure choices can be distorted between competing industries. Promoting competitive infrastructure markets is desirable, where feasible, as it promotes efficient use of, and investment in, infrastructure and reduces the need for regulated pricing. New entrants and effective competition between existing players also can play a critical role in lifting productivity and stimulating the introduction of innovative new technologies, services and practices in the provision of infrastructure.

As noted in Statement 3, global demand for resources has increased significantly over recent years. Supply responses typically have lags because of the large fixed costs inherent in mining projects and significant volatility in commodity prices. There has consequently been little spare capacity to meet increased demand and prices have increased significantly. In response to rising prices, Australian mining investment has surged and the resulting increase in output has begun to lift export volumes.

As a result, the resource boom has put pressure on the capacity of some key east coast rail lines and ports. However, concerns have also been expressed about systemic, long-term capacity constraints emerging in electricity, rural and urban water and interstate freight and urban passenger road and rail networks (Business Council of Australia 2005; Productivity Commission 2005b).

Despite the many productivity and cost gains delivered during the past two decades, a further set of initiatives could build on these gains. Such initiatives could encourage competition, improve incentives for investors to install appropriate new infrastructure facilities and encourage their more efficient use. Successful reforms could boost national productivity significantly. In 2005 the Council of Australian Governments will review ongoing arrangements for National Competition Policy. The Australian Government initiated the Productivity Commission review to inform this process.

The role of government

Governments alone cannot resolve every problem and achieve every political, economic and cultural objective of society. In most cases private markets, individuals and communities will be better placed to meet the objectives they are seeking. In some instances governments are best placed to act, while other cases will require public and private cooperation.

As such, governments face a continuing challenge in defining the scope of their roles and in performing efficiently and effectively. Yet Australia's prosperity depends on the sound use of scarce resources in both the public and private sectors.

Governments can support productivity growth in the broader economy through efficiently managing public sector agencies to deliver services to the public in an effective manner. They also have a role in improving the efficiency of private markets by setting regulations that provide a framework for, and secure confidence in, market operations. Competitive forces will continue to drive ongoing productivity improvements. In Australia's federal system of government the rate of productivity growth in both the public and private sectors also depends on the effectiveness with which the three levels of government work together.

By establishing sound frameworks for decision-making and resource allocation, well-governed institutions and markets reduce the risk of economic instability and the vulnerability of the economy. They help contain the shocks to which an economy is exposed, making it easier for firms and households to adjust. Despite being exposed to the large negative external shocks of the East Asian financial crisis, for example, Singapore and Australia fared relatively well. This was due partly to sound governance arrangements within public institutions and domestic economies (Johnson et al 2000; de Brouwer 2003).

Governance

Governance is one key area where governments can act to improve productivity. Governance covers the set of arrangements by which those managing an organisation are accountable to those with a legitimate interest in the organisation.

Improving governance standards for companies is the focus of the Corporate Law Economic Reform Program (CLERP). The objective is to boost investor confidence that boards and management will make sound decisions and increase the return on shareholder funds for the ongoing benefit of shareholders, employees and the wider community.

In the public sector, governance is about how parliaments, governments, boards and public service managers relate to each other and are answerable for the cost-effective performance of public functions and the delivery of public services. Reforms have strengthened financial and accountability arrangements and sharpened the focus on effective public service delivery. The reforms have included introducing the Charter of Budget Honesty, new financial management legislation, whole-of-government budgeting, reporting on an accrual basis, and strengthened performance reporting and benchmarking requirements.

That said, the best policies in the world will not deliver the intended outcomes if government agencies do not implement them in the manner governments intended. While some steps have been taken to improve arrangements between the Australian Government and its agencies, the Review of the Corporate Governance of Statutory Authorities and Office Holders (Department of Finance and Administration 2003), also known as the Uhrig Review, found governance could be enhanced by providing greater clarity in the relationships between Ministers, their departments, the Parliament, the public, statutory authorities and office holders.

The Uhrig Review developed templates of best practice governance principles. The application of those principles is intended to provide statutory authorities and office holders with clear purpose and guidance about government expectations and objectives. The governance arrangements of Australian Government statutory authorities and office holders are to be assessed against the templates by March 2006. Assessments are continuing, with implementation of the recommendations to occur on a rolling basis by March 2007.

Australian Government and state relations

The effective and productive delivery of government services also is affected significantly by the relationship between the three levels of government, and particularly between the Australian Government and the states. This is because they are jointly involved in almost every functional area of government, with the exception of defence.

The Australian Government has sound reasons for involvement in many functional areas. They include promoting national standards, ensuring coordination and achieving national objectives such as enhanced productivity and participation. Similarly, state governments have sound reasons for involvement. However, joint government involvement in the same functional areas raises significant challenges including complexity for the public, cost and blame shifting, and possible duplication or gaps in service delivery.

In the medium term, all tiers of government will face significant pressure from the ongoing effect of cost drivers including demographic change. The Productivity Commission (2005a) projects that the aggregate fiscal pressure for all governments associated with the ageing population could be over 6 per cent of GDP by 2044-45 with the bulk of this expected to be borne by the Australian Government, but state governments face pressures as well. Growing spending pressures in key areas of service delivery accentuate the need to ensure that service provision is as effective and efficient as possible.

Some recent progress has been made in improving the allocation of the roles and responsibilities of governments. In addition, the introduction of the GST provided the states with a growing source of revenue. This enabled states to abolish a range of inefficient taxes and provided them with more funding certainty to meet their responsibilities.

Going forward, it will be important for the Australian Government and the states to clarify roles and responsibilities in order to improve productivity in the provision of services to the public while sustaining government finances. Clarification of roles will require consideration of national strategic priorities and judgements as to the tier of government that is likely to discharge those priorities most effectively.

Complexity and uncertainty

Complexity and uncertainty increase as markets expand beyond state and national borders. This can add to the cost of transactions and thereby limit the potential opportunities for increased investment and consumption.

Government intervention through the rule of law provides a framework to reduce uncertainty by providing greater confidence that private transactions will be completed satisfactorily. Through regulation, revenue raising activities and spending decisions, governments may add to or reduce the complexity faced by market participants. For example, governments might reduce complexity by requiring providers of similar products to promote or advertise them in a consistent, easily comparable manner.

On the other hand, contradictory regulations across sub-national levels of government can add to the difficulty of doing business. Addressing such issues was behind the Australian Government's drive to set consistent regulation of corporations and the securities and financial systems. It is also an important driver of the Australian Government's intention to develop a uniform approach to workplace relations.

In many cases, market participants can assist in managing complexity, thereby helping individuals to deal with complex information, procedures or regulation.

Governments may add unnecessarily to complexity by over-regulation, by setting ineffective or inappropriate regulation or policies, or by too frequently changing them. Over-regulation might arise, for example, when government decision-making is heavily influenced by the demands of the most risk averse, or where the concern being addressed is not fully understood by regulators. The Australian Government has sought to reduce the likelihood of such outcomes through the establishment of a number of consultative arrangements, including the Board of Taxation and the Financial Sector Advisory Council, and by consulting with business and consumer groups when developing legislation.

The design of policies and the way that laws and regulations are crafted also can add unnecessarily to complexity. For instance, attempts to cover in detail all current possible treatments in the law may require constant updates and additions as society and markets continue to evolve. In such circumstances principle-based drafting of laws and regulations may be more appropriate. Policy measures also can be incremental, adding one layer of complexity to another. On occasions more comprehensive policy redesign may overcome decades of built up complexity.

Australia's tri-level system of government and our need to integrate with the global community influence the levels of complexity Australians face and the impact of this complexity on market efficiency. For example, recent reports by both the Productivity Commission (2005b) and the Business Council of Australia (2005) have concluded that differing greenhouse policies between jurisdictions are imposing costs, creating uncertainty and impeding investment in Australia's infrastructure. As another example, businesses that operate across states and self-insure for workers' compensation face added costs from complying with different related financial and prudential requirements in each jurisdiction.

Maintaining our natural environment

Continued economic growth and prosperity require sound management of the natural environment. Clean water, clean air, arable land and sustainable timber stocks for example are essential to the productive capacity of almost all sectors within the Australian economy. The natural environment also provides important recreational and other benefits that, despite being less tangible in a financial sense, still make a valuable contribution to the wellbeing of Australians.

Until recent decades, there has been a lack of understanding of the role that Australia's unique environment plays in supporting the economy. The seeming limitless nature of Australia's natural environment meant it had sometimes been undervalued. Pressures on the environment are manifest in problems such as salinity, concerns over water quality and quantity, and issues surrounding greenhouse emissions.

Over time Australians have increasingly come to value the environment more highly and to seek solutions to environmental challenges. In response Australian Government expenditure on the environment has increased substantially in recent years and is budgeted to reach $3.2 billion in 2005-06. This budget builds on flagship environmental programmes such as the Natural Heritage Trust and the National Plan for Salinity and Water Quality. It establishes the $2 billion Australian Water Fund, commits an additional $181 million to protecting Australia's fisheries in the Southern Ocean from over-fishing and provides an additional $100 million for environmental research.

Unlike most other scarce commodities, there are no effective markets for many environmental goods and services. This reflects factors such as a lack of clear property rights, the existence of externalities and the public good characteristics of the environment. As a result, users of the goods and services provided by the natural environment often have faced little incentive to recognise the costs that they have imposed, given the alternative uses to which natural resources could have been put. Where this has occurred, it is likely that environmental resources have been used in ways that have not been economically efficient and which have failed to recognise their potential contribution to community amenity. In many instances, inefficient use of environmental resources has contributed to environmental degradation.

The inefficient use of environmental resources can constrain economic productivity and prevent future generations from enjoying the same high levels of environmental benefits that Australians enjoy today. A commonly cited example where this could occur is if water catchments were allowed to become degraded. The 'free' water filtration provided by the environment then would need to be replaced with expensive water filtration plants, thereby diverting workers and capital from alternative productive activities.

With demographic factors placing increased pressure on government budgets, sustainable resource use will need to be governed mainly by market incentives and regulatory approaches rather than by direct government spending. A key benefit of market-based approaches is that they seek to correct the underlying market failures that lead to environmental degradation. Market-based approaches provide a clear incentive to use environmental resources efficiently and to seek out more innovative production techniques.

By using markets to solve environmental problems, economic growth and higher living standards need not be at odds with improved environmental outcomes. Internationally, markets are increasingly likely to be used to manage the environmental impacts of nitrous oxide, sulphur and greenhouse gas emissions and to support conservation. Reflecting Australia's particular circumstances, opportunities for the innovative use of environmental markets are being examined on a case-by-case basis in areas such as fisheries, native vegetation and salinity.

A significant example of a market solution is the National Water Initiative (NWI), which was agreed in June 2004 by the Australian Government and most states. A key objective of the NWI is to establish a clearly defined property rights framework for water and the creation of effective water markets. The price signals created by such markets will provide incentives for water to be transferred to its highest value use. This will encourage investment in water-efficient technology and infrastructure that will be needed to sustain Australia's future economic growth. At the same time, the property rights and water planning frameworks included in the NWI will be based on best available scientific knowledge so that water use is more consistent with environmental sustainability.

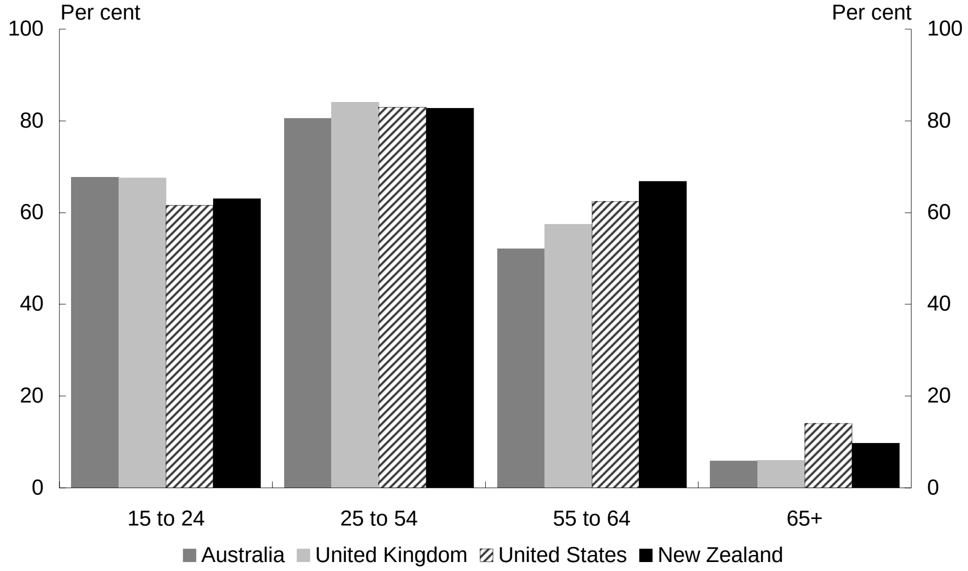
IMPROVING PARTICIPATION AND SHARING AUSTRALIA'S PROSPERITY

Households contribute to and share in the benefits of an increasingly prosperous Australia.

The entire community benefits from the output produced through work. This is true whether work is for an income or not. Many people gain a sense of worth from their work and enjoy greater opportunities for social engagement, which enhance both mental and physical wellbeing. Though not normally recorded in economic statistics, unpaid work within the home and by unpaid carers and volunteers contributes significantly to the community. Voluntary work is also an important path to paid employment for many people. Almost one-third of Australian adults undertake some form of voluntary work, contributing an average of more than 3 hours per week (ABS 2001). It is through paid work, however, that most people support their pre-retirement lifestyles and save for retirement, while contributing to measured economic growth.

The ageing of the population will slow the growth in living standards in coming decades unless productivity growth and labour force participation rates increase. Australia's overall labour force participation rate, the 12th highest in the OECD, remains modest by international standards (OECD 2004a). Labour force participation in Australia decreases markedly in older age groups. Some people retire or leave the workforce in their forties and fifties. While declining participation is consistent with the trend in other OECD nations, total participation in Australia for those aged 55 years and older is lower than the OECD average and well below that in the United States, United Kingdom and New Zealand (Chart 7).

Chart 7: Labour force participation rate by age, 2003



Source: OECD (2004a).

While the nature and extent of workforce participation is largely a matter of individual choice, such choices may be distorted by disincentives or obstacles to participation that impose unnecessary costs on individuals and society. Since 1996, the Australian Government has implemented a range of policies to support an individual's choice to engage in the labour force and remove disincentives to such participation. Among those policies are workplace relations reform, increasing assistance with child care, reforms to the income support and family assistance systems, income tax reductions and changed superannuation arrangements. Those reforms have helped improve participation rates.

Going forward, the ageing population will require even higher rates of participation. The Australian Government has identified three broad categories of policy reform that should promote higher participation rates:

- strengthening an individual's capacity to work through better health and education;
- improving incentives and removing barriers to undertake work, through welfare reform and creating more flexible and adaptable retirement income arrangements; and
- increasing the flexibility of the labour market, to facilitate greater employment options and encourage job creation.

While the full benefit of many of those reforms may not be measured for some time to come, they underpin and set the tone for ongoing efforts required to sustain current growth rates in Australia's standard of living.

Strengthening capacity

Education and training systems provide the skills and flexibility the workforce needs to meet the requirements of an increasingly dynamic and complex economy. Illness and injury, on the other hand, reduce workforce participation and limit lifestyle choices and overall wellbeing.

A skilled workforce

Education plays a critical role in allowing people to participate more fully in society. Education also has costs in terms of both the financial cost of acquiring the education and the time that students otherwise could have spent working or enjoying leisure. As with any investment, more is not always better. Education will be most effective when individuals and societies invest in the right people, the right skills and at the right time.

Australians have been investing steadily more time and effort into education (Box 2). Surveys suggest that higher levels of education and training are likely to increase labour force participation over time. In 2001 the labour force participation rate for people aged 25 to 64 with post-school qualifications was 85 per cent, but only 63 per cent for people who had no post-school qualifications (ABS 2003). Unemployment rates are also far lower for people with post-school qualifications.

Box 2: Australia's qualifications profile

Australians have become more highly qualified over the past few decades (Table 1). While older Australians are less likely to have been educated beyond lower secondary school than their peers within the rest of the OECD, the qualifications profile for younger Australians is very similar to their OECD counterparts.

Australia's overall qualifications profile is hollow in the middle. Fewer Australians complete upper secondary education than in the rest of the OECD, while more Australians hold either tertiary or only lower secondary qualifications. However, the qualifications profile for 25 to 34 year olds suggests this may be changing. Current upper secondary retention rates suggest that younger cohorts will be at least as well-qualified as 25 to 34 year olds are today.

Table 1: Highest qualification obtained, per cent by age group, 2002

	Age group				
	25-34	35-44	45-54	55-64	Total
Australia					
Tertiary	35.8	31.2	30.5	22.5	30.8
Upper secondary(a)	36.7	30.7	27.3	23.2	30.2
Lower secondary	27.5	38.1	42.2	54.3	39.1
Rest of OECD(b)					
Tertiary	30.7	26.9	25.1	19.0	26.0
Upper secondary(a)	43.8	44.1	42.7	38.3	42.6
Lower secondary	25.5	29.0	32.2	42.7	31.4
Difference(c)					
Tertiary	5.1	4.3	5.4	3.5	4.8
Upper secondary(a)	-7.1	-13.4	-15.4	-15.1	-12.4
Lower secondary	2.0	9.1	10.0	11.6	7.7

(a) Includes post-school non-tertiary qualifications.
(b) Excludes Luxembourg.
(c) Percentage points.
Source: Australian Government Treasury calculations based on OECD (2004a).

Education and training also support high levels of productivity. More highly trained employees are likely to be more innovative, developing and using new ideas and technology that can lead to new and better products or more efficient ways of working.

The Australian Government has implemented initiatives in recent years aimed at improving educational and skill attainment across all age groups. Ongoing reforms have enhanced greatly the scope, consistency and labour market responsiveness of the vocational education and training system. Participation in vocational education and training has grown strongly.

The Australian Government is building on earlier initiatives by establishing 24 Australian technical colleges, expanding school-based new apprenticeships, increasing pre-vocational training places and increasing income support for new apprentices.

The Australian and state governments are negotiating new vocational education and training agreements to increase the flexibility of the training system. Planned reforms include removing impediments to user choice so that employers and employees have greater freedom to choose the training organisation that best suits their needs. Reforms also are designed to improve the responsiveness of the training system to emerging skill shortages by creating 20,000 new targeted training places.

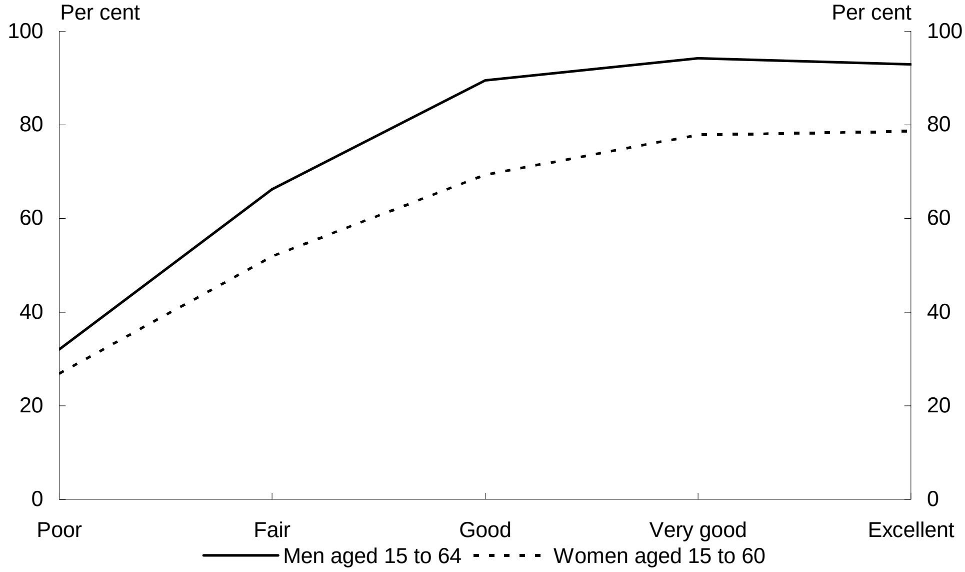
Even so, sometimes shortfalls in the supply of skilled workers may emerge for which the optimal solution may be targeted immigration. At such times, skilled migration is a useful complement to education and training initiatives. Skilled migration provides a rapid boost to the national skills pool, whereas education and training initiatives take longer to deliver skilled workers to the labour market. Accordingly, the Government will increase skilled migration in 2005-06 by 20,000, delivering a total skilled migration intake of 97,500.

A healthy workforce

In general, healthier people are likely to be more productive and have higher labour force participation rates, leading to potentially higher disposable incomes, wealth and general wellbeing (Chart 8). Healthier people are also more likely to respond positively to incentives to remain in the labour force beyond traditional retirement ages, participate in voluntary positions within the community upon retirement and require less assistance later in life. Deteriorating health is often associated with early retirement.

Employers also benefit from healthier workforces, not only through increased labour force participation and productivity, but from the reduced costs of lower rates of absenteeism due to ill health or disability. The community benefits from the fewer resources needed for health care and more widespread community engagement.

Chart 8: Labour force participation rate by health status



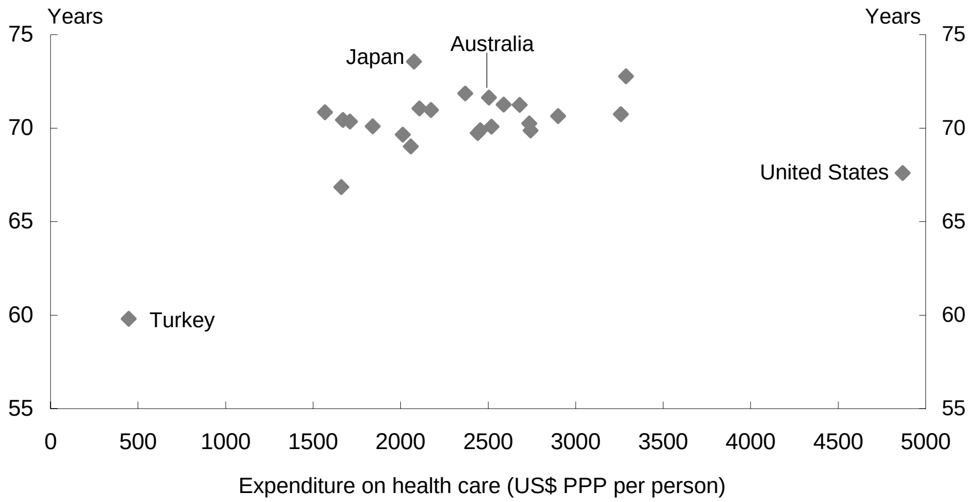
Source: Cai and Kalb (2004).

Chronic diseases, such as heart disease, cancer and diabetes directly reduce the wellbeing of sufferers and their carers, and have an adverse effect on the prosperity of the community through reduced participation and productivity. Those diseases are among the leading causes of death in Australia, yet many of them have preventable risk factors related to lifestyle, including tobacco use, excess consumption of alcohol, unhealthy diet and physical inactivity.

Australians are living longer, but have more health concerns. While life expectancy at birth increased from around 73 years in the latter half of the 1970s to 80 years in 2001, the proportion of Australians reporting long-term health conditions rose from 45 per cent to 78 per cent over this period (ABS 2002, 2004c; Australian Institute of Health and Welfare 2000). The trend is partly due to the increasing prevalence of lifestyle-related diseases and partly due to the development of treatments that alleviate previously fatal conditions.

Similar developments have increased health care expenditure in most OECD countries in recent decades. However, perhaps surprisingly, the level of health expenditure across OECD countries is not strongly correlated with the health of their populations (Chart 9). Australians enjoy longer, healthier lives than the populations of many countries, such as the United States, that spend more on health care. This suggests that better health outcomes are not necessarily the result of more expenditure and that factors such as the structure of the health system and active and healthy lifestyles can be more important.

Chart 9: Healthy life expectancy and health care in 24 OECD countries, 2001



Source: OECD (2004c); and WHO (2002).

Ultimately, individuals, families and communities make the lifestyle choices that can lead to the development of chronic disease. Governments cannot proscribe choices, but they can provide incentives and sanctions to encourage healthier lifestyle choices. For example, governments have imposed high excises on tobacco and restricted where people are permitted to smoke. In other areas there may be limited scope for incentives or sanctions, but governments have a role to provide relevant health promotion information. Governments also can aim to have a broad range of policies and programmes — including public transportation, parks, school curricula, town planning, as well as the health care system — that support healthy lifestyle choices.

The most cost-effective approach to many chronic illnesses is likely to be a population strategy that raises awareness, changes social attitudes and improves lifestyles, thereby removing or reducing the underlying causes that make the disease common (WHO 2002, 2004). With changing community attitudes, the maintenance of healthier lifestyles becomes easier for any particular individual as the healthier behaviour becomes more common place (Rose 1985, 1994).

The 2004 Building a Healthy, Active Australia package aims to promote better population health by encouraging children to adopt healthy habits for life. Analyses by Rose and the WHO suggest such programmes are likely to be even more effective in changing social attitudes were they extended to involve families and the entire community.

Improving incentives and removing barriers

While decisions to participate in the paid or unpaid workforce are necessarily personal they have impacts on the wellbeing of the nation through the relationship between participation, economic growth and prosperity. These decisions are influenced by provision of income support, tax arrangements, retirement incomes policies and other incentives and barriers to participation.

Income support systems provide a social safety net. They also should aim to recognise an individual's desire to work by encouraging, promoting and assisting them to seek out and participate in paid work to the extent they are able. The challenge for government is to balance the set of incentives, assistance and requirements in such a way as to avoid creating cycles of dependency, while maximising the voluntary participation of people with diverse capacities and availabilities for work.

While labour force participation is currently at historic high levels, there is room for further improvement. Of the 14 million people aged 15 to 64 years, only about 10 million are currently in the labour force. Around 2.7 million receive income support, including sole parents, the unemployed and recipients of the Disability Support Pension (DSP).

Welfare system reforms and income tax reductions have improved the incentives to participate for most income support recipients. The 2004-05 More help for families package improved incentives for people to participate in the workforce. The 2001-02 Australians Working Together package included reforms to assist out-of-work people back into the workforce. They included introducing working and training credits, mutual obligation requirements for some job seekers and initiatives targeting parents, the mature aged, indigenous Australians and people with disabilities. Many of these groups of people have lower than average participation rates.

Despite the progress to date, more could be done to match incentives with individuals' capacities to contribute. Currently, only around one in six income support recipients are required to look actively for work. While a proportion of the remainder are involved in other important activities, such as education and family-related commitments, more income support recipients could participate in the labour market. This would improve the longer-term economic and social wellbeing of the individuals concerned and add to the prosperity of the community.

The OECD (2005a) has noted that the DSP, in part due to its generosity, may be used by some as an early retirement vehicle. It is paid at the same rate as the Age Pension and is significantly higher than unemployment benefits. More than 40 per cent of all DSP recipients in June 2004 were aged 55 or older, with just over 20 per cent of all recipients aged 60 or older.

In this budget, the Australian Government introduces additional reforms to the income support system to encourage further labour force participation. The further reform of the welfare system in this budget focuses on assisting those who have the capacity to work to do so, while maintaining an appropriate level of assistance to provide a minimum standard of living. The reforms achieve this through a balance of financial incentives, obligations to look for work and a broad-ranging package of services to assist those who have been out of the workforce for an extended period.

An individual's decision to participate in the labour force is affected by both the additional income tax paid and the withdrawal of income support payments through income testing arrangements. Taken together, the interactions are described as effective marginal tax rates (EMTRs), although of course they are not actual tax rates.

EMTRs have fallen in recent years largely through reduced income tax rates and reduced family assistance taper rates. The changes particularly assist women wishing to re-enter the workforce after having children. In addition, the increase in thresholds for the top marginal tax rates has improved incentives for some workers to take on additional work, seek promotion and invest in further skills.

In this budget the Government has taken further steps to reduce EMTRs through relaxation of the income test for Newstart Allowance. This will reduce the current 70 per cent withdrawal rate to 60 per cent and increase the range of income over which the 50 per cent withdrawal rate applies.

With an ageing population, any improvement in the labour force participation of mature age workers will help sustain growth and prosperity. Governments can encourage and support individual choices to stay in the workforce beyond traditional retirement age.

It is very difficult to reverse retirement decisions, once taken (OECD 2003). Policy may more effectively encourage people still in the workforce to delay retirement. Consistent with this, the Australian Government has introduced a number of initiatives to encourage older workers to remain in the workforce, including tailored services to assist mature age job-seekers to find new employment and flexible assistance to help parents, carers or mature age people to find work. It also has removed the restriction on access to superannuation by those still in employment, enabling older workers to move gradually into retirement by supplementing reduced employment earnings with their superannuation entitlements. For workers older than 55 years the Australian Government has introduced the Mature Age Worker Tax Offset that provides an annual tax rebate of up to $500 on earned income.

Together those reforms are likely to have contributed to the recent increase in the labour force participation rates of those aged 55 years and older.

Enhancing flexibility

Through reform, what was a highly centralised and regulated workplace relations system in Australia has moved to one more focused on agreement making at the workplace or enterprise level. Today, only around 20 per cent of workers have their pay and conditions set directly by awards (ABS 2005d). This significant change has increased enterprise flexibility and competitiveness and has contributed to the Australian economy's strong employment and economic growth over recent years.

Employees also can more easily negotiate working arrangements that suit their other commitments or lifestyle choices. The number of people choosing to work part-time has increased rapidly and this trend is likely to continue as the population ages.

The reforms provide a firm foundation, but there remains significant scope to do more. Greater flexibility in employment arrangements and conditions would promote workplace productivity and allow employers and employees to tailor wages and conditions to their specific skills and needs. This creates greater opportunities for people to find jobs, increase their incomes and respond positively to changing industry demands for labour.

The Australian Government has proposed further changes to workplace relations that reduce the degree of regulation around the termination of employment, address pattern bargaining, streamline agreement-making processes and simplify awards to promote workplace agreements.

MAINTAINING A DISCIPLINED APPROACH TO FISCAL POLICY

The challenges Australia faces in sustaining its economic performance will shape the direction of fiscal policy in the years ahead. The challenges will translate into additional pressures on public finances and will influence future decisions about the content of government expenditure programmes and the structure of the tax system.

As with households, governments must manage budgets so they can meet their financial commitments, including regular expenses and debt repayments, from current and expected future income. In many other developed countries, this will mean cutting spending or raising taxes to reduce government debt to levels that can be serviced through future tax and other government revenues.

Fortunately Australia does not face such stark choices. Responsible management of revenue and expenditure has resulted in a succession of budget surpluses. Those surpluses have been used to repay debt. Government debt is now at levels that are among the lowest in the OECD (OECD 2004b).

The task going forward is to ensure that policies safeguard the sound fiscal position and that budgetary decisions are consistent with promoting productivity and participation. This means maintaining a responsible approach to government expenditures and securing a tax base that can fund those expenditures in an efficient and equitable manner. It also means managing pressures and risks to revenue or expenditure so future governments can continue to provide essential goods and services in a manner that promotes fairness in distributing public resources between generations of Australians. Maintaining a responsible fiscal position is important to maintaining low inflation and low interest rates today, thereby providing a more stable environment for households and firms to make investment decisions.

The ageing population, technological advancement in health care and rising community expectations about access to the latest medical treatments are likely to place significant pressure on government finances. In addition, pressure on public finances is likely to come from increasing community expectations around maintenance of our natural and man-made environment.

Maintaining a sound fiscal position will require governments to design programmes with a view to promoting productivity and participation, thus securing the viability of their revenue base. It will also require improved allocation of functions and coordination of programme delivery across the three levels of government so that publicly provided goods and services are delivered as efficiently and effectively as possible. A particular challenge in this regard will be to coordinate an approach to the delivery of infrastructure that pays regard to the appropriate balance between public and private provision, and develops the regulatory environment needed to support the latter.

Governments at all levels also will need to take a broader view of their balance sheets, taking greater account of the need to meet contingent liabilities and future pressures on the tax base and expenditures. As discussed in more detail in Statement 2, the Australian Government is taking steps to help offset the liability associated with unfunded public sector superannuation by establishing the Future Fund, comprising financial assets built up using current and future budget surpluses.

A key outcome of funding the superannuation liability will be to improve the Australian Government's net worth and financial sustainability. It will also change the measurement of financial performance — giving more attention to the evolution of the Australian Government's assets and liabilities over time, rather than simply current receipts and payments.

An approach to fiscal policy that focuses more clearly on improvements in the balance sheet recognises that many of the fiscal pressures governments face will arise decades into the future. The production of the 2002 Intergenerational Report, which assessed expenditure pressures, was an important first step in this direction. Ensuring fiscal sustainability will require longer term planning horizons than have been employed in the past. This requires a view of the likely path of the budget aggregates and a more detailed understanding of how individual programmes may contribute to fiscal pressures over the medium to longer term.

The sustainability of fiscal policy depends not only on decisions made in the budget, but on the range of economic and social policies needed to provide higher income levels into the future. Critically, Australia needs to take advantage of opportunities to secure higher national income through trade, including with growing economies such as China and India. Australia's current fiscal position in part reflects the dividends of a positive international engagement strategy.

This budget has responsibly banked some of the additional revenue generated by higher export prices to help meet the fiscal challenges ahead.

CONCLUSION

The sustained strong performance of the Australian economy over the last decade has meant that Australians are enjoying increased prosperity and wellbeing. The strong performance has been underpinned by a sustained reform effort aimed at improving productivity and labour force participation.

The strong economy, combined with a sound fiscal outlook, presents a unique opportunity to develop and implement a cohesive policy agenda for making even better use of our natural, man-made and human resources, thereby locking in future growth and prosperity. The opportunity should not be wasted because strong growth and sound policies will be the best weapons against the impact of an ageing population and other future known and unknown challenges.

Some of those policies will build on and refine past reforms. Some challenges will take policy into new areas or new directions. In all areas, the challenge is to identify barriers to sustained economic growth and to engage individuals, businesses and governments in implementing appropriate solutions.

The success with which governments implement such policies, and how well individuals and businesses respond to them, will determine the extent to which Australia achieves strong economic growth and prosperity now and over the decades to come.

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PART 3
REVENUE, EXPENSES AND BUDGET FUNDING

This part discusses the changes in the revenue outlook since the 2004-05 MYEFO.

This part examines short to medium term trends in the expenses and net capital investment estimates. The changes since the 2004-05 Budget and MYEFO are also detailed.

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

This part also discusses the management of Australian Government debt including the impact of the Future Fund.

STATEMENT 5: REVENUE

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

The Australian Government is providing further cuts to personal income tax of $21.7 billion over 4 years and will abolish the superannuation surcharge from 1 July 2005.

The revenue estimates for 2005-06 have been revised up since the *Mid-Year Economic and Fiscal Outlook 2004-05*, reflecting a stronger outlook for employment, company profits and the incomes of small unincorporated businesses and personal investors. As a result of actual revenues exceeding forecasts over recent years, methodology changes to the forecasts have been made to improve accuracy.

Information about GST revenue is provided in Budget Paper No. 3, *Federal Financial Relations 2005-06*.

Appendices

STATEMENT 5: REVENUE

OVERVIEW

Relative to the *Mid-Year Economic and Fiscal Outlook 2004-05* (MYEFO), total revenue for 2005-06 is expected to be higher, with stronger growth in income taxation revenue from companies, small unincorporated businesses and personal investors. Personal income tax cuts of $21.7 billion over 4 years will commence on 1 July 2005. These tax cuts are in addition to those announced in the 2004-05 Budget. The superannuation surcharge will be abolished from 1 July 2005.

Revenue forecasts[1] for 2004-05 and 2005-06 along with projections for the period from 2006-07 are provided in Table 1.

Table 1: Total Australian Government general government revenue

	Actual	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
Total taxation revenue ($b)	**175.1**	**190.2**	**201.3**	**209.0**	**218.8**	**230.1**
Real growth on previous year (%)	3.5	4.6	1.2	3.1	4.0	3.2
Per cent of GDP	21.5	22.0	21.7	21.6	21.7	21.7
Non-taxation revenue ($b)	**12.5**	**12.5**	**13.2**	**13.9**	**14.6**	**15.2**
Real growth on previous year (%)	0.9	-4.0	1.7	4.1	4.5	2.1
Per cent of GDP	1.5	1.4	1.4	1.4	1.4	1.4
Total revenue ($b)	**187.6**	**202.7**	**214.5**	**222.9**	**233.4**	**245.3**
Real growth on previous year (%)	3.3	4.0	1.3	3.2	4.0	3.1
Per cent of GDP	23.1	23.5	23.1	23.0	23.2	23.1

Total revenue is projected to decrease from 23.5 per cent of GDP in 2004-05 to 23.1 per cent in 2008-09. The decrease in revenue as a share of GDP is mostly due to a decrease in taxation revenue, which is projected to fall from 22.0 per cent of GDP in 2004-05 to 21.7 per cent in 2008-09.

1 All revenue estimates in this statement are reported on an accrual basis unless otherwise specified. A summary of the tax system is provided in Appendix A. Commentary on accrual and cash taxation revenue is provided in Appendix E. Detailed estimates on a cash basis are provided in Appendix C. Historical receipts outcomes are provided in Appendix G. 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 is provided in Budget Paper No. 3, *Federal Financial Relations 2005-06*.

VARIATIONS IN THE REVENUE ESTIMATES SINCE THE 2004-05 BUDGET

Table 2 is a reconciliation of this Budget's revenue estimates with those at the 2004-05 Budget and the 2004-05 MYEFO.

Table 2: Reconciliation of total Australian Government general government revenue estimates from the 2004-05 Budget and the 2004-05 MYEFO

	Estimates		Projections	
	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m
Revenue at 2004-05 Budget	**193,151**	**201,383**	**212,199**	**223,129**
Changes between 2004-05 Budget and MYEFO				
Effect of policy decisions	-11	-401	-1,115	-1,024
Effect of parameter and other variations	6,303	6,514	6,486	7,237
Total variations	6,292	6,114	5,371	6,213
Revenue at 2004-05 MYEFO	**199,443**	**207,497**	**217,570**	**229,341**
Changes between MYEFO and 2005-06 Budget				
Effect of policy decisions	-35	-3,472	-6,675	-7,662
Effect of parameter and other variations	3,258	10,486	11,986	11,725
Total variations	3,223	7,014	5,311	4,064
Revenue at 2005-06 Budget	**202,666**	**214,511**	**222,882**	**233,405**

Total revenue for 2004-05

Relative to MYEFO, estimated total revenue for 2004-05 has been revised up by $3.2 billion, largely owing to higher expected revenue from wage and salary earners, personal investors and small unincorporated businesses.

Total revenue for 2005-06

Total revenue for 2005-06 has been revised up by $7.0 billion since MYEFO, reflecting higher estimated revenue from companies, personal investors and small unincorporated businesses. These upward revisions have been partly offset by the impact of the Government's decision to provide personal income tax cuts.

Effect of policy decisions

Policy decisions since the 2004-05 MYEFO are expected to reduce taxation revenue by around $3.5 billion in 2005-06 and around $26.1 billion over the forward years (a more detailed description of these is provided in Budget Paper No. 2, *Budget Measures 2005-06*).

In particular, the Government's decision to provide personal income tax cuts will reduce revenue by $3.1 billion in 2005-06, and $21.7 billion over the forward estimates period. The tax cuts will take effect in two stages.

- From 1 July 2005, the 17 per cent rate will be reduced to 15 per cent, the 42 per cent threshold will be increased from $58,001 to $63,001 and the 47 per cent threshold will be increased from $70,001 to $95,001 (compared with $80,001 announced in the 2004-05 Budget).

- From 1 July 2006, the 42 per cent threshold will be further increased to $70,001 and the 47 per cent threshold will be further increased to $125,001.

These tax cuts will increase disposable incomes and improve the incentives for all Australian taxpayers to participate in the workforce. Moving the 42 per cent threshold up to $70,001 means that more than 80 per cent of taxpayers will face a top marginal tax rate of no more than 30 per cent over the forward estimates period. Substantially raising the thresholds for the top two marginal tax rates will also improve work incentives.

The Government's personal tax cuts package will also ensure that senior Australians in the community will be better off with an increase in the Medicare levy threshold that applies to them. This measure has been specifically designed to ensure that senior Australians do not pay the Medicare levy until they begin to incur an income tax liability.

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

- The superannuation contributions and termination payments surcharge will be abolished for contributions made from 1 July 2005, with a cost to revenue of $650 million in 2006-07 and $2.5 billion over the forward estimates.

- The 3 per cent tariff applying to business inputs imported under a tariff concession order will be removed with effect from 11 May 2005, with a cost to revenue of $36 million in 2004-05, $290 million in 2005-06 and $1.3 billion over the forward estimates.

- The eligibility criteria for the mature age worker tax offset will be extended from 2005-06, with a cost to revenue of $70 million in 2005-06 and $295 million over the forward estimates.

- A four-year income tax exemption will be provided for temporary residents for most foreign source income, including capital gains, commencing from July 2006, with an estimated cost to revenue of $50 million in 2007-08 and $105 million over the forward estimates.

- The capital gains tax treatment of non-resident investors in Australia will be aligned more closely with international standards, with a cost to revenue of $50 million in 2005-06 and $230 million over the forward estimates.

- Certain currently unrecognised business capital expenditures ('blackhole expenditures') will be recognised for tax purposes from 2006-07 with a cost to revenue of $35 million in 2006-07, increasing in later years, with a cost of $205 million over the forward estimates.

- The capital allowance treatment of film copyright will be changed to ensure the application of the effective life depreciation regime, with effect to expenditures after 1 July 2004, with a cost to revenue of $15 million in 2005-06 and $175 million over the forward estimates.

- Foreign loss and foreign tax credit quarantining will be abolished, with effect from the first income year after Royal Assent, with an estimated cost to revenue of $25 million in 2007-08 and in 2008-09.

A detailed description of the policy decisions is provided in Budget Paper No. 2, *Budget Measures 2005-06*. A summary of revenue policy decisions since the 2004-05 MYEFO is provided in Table 3.

Table 3: Revenue policy decisions since the 2004-05 MYEFO

	2004-05 $m	2005-06 $m	2006-07 $m	2007-08 $m	2008-09 $m
Revenue policy decisions					
Personal income tax cuts		-3,100	-5,600	-6,250	-6,700
Superannuation surcharge abolition		-	-650	-875	-990
Tariff concessions – removal of 3 per cent tariff on business inputs	-36	-290	-300	-320	-340
Mature age worker tax offset - extended definition of net income from working		-70	-75	-75	-75
Foreign income exemption for temporary residents		-	-	-50	-55
Reforms to the capital gains tax treatment of non-residents		-50	-50	-65	-65
Not proceeding with the generic regime for the taxation of rights		35	50	55	65
Taxation treatment of business 'blackhole' expenditure		-	-35	-70	-100
Inclusion of film copyright in the effective life regime		-15	-35	-55	-70
Increasing the Medicare levy low income thresholds		-38	-19	-18	-18
Biometrics for border control - progressive introduction of ePassports		11	19	20	21
Other revenue policy decisions	1	45	20	41	22
Total revenue policy decisions	**-35**	**-3,472**	**-6,675**	**-7,662**	**-8,305**

Effect of parameter and other variations

Parameter and other variations are expected to increase revenue in 2004-05 by $3.3 billion, and revenue in 2005-06 by $10.5 billion, relative to the MYEFO forecasts.

Parameter variations

Since MYEFO, estimated nominal GDP growth in 2004-05 has been revised down by ½ of a percentage point, but taxation revenue growth has been revised up by 1½ percentage points. The strength in taxation revenue is largely the result of stronger than expected employment growth in the second half of 2004, improved income for small unincorporated businesses and additional strength in individuals' realised capital gains and other income.

Looking ahead, there have been significant upward revisions to revenue in 2005-06 and the projection years since MYEFO, reflecting the flow on effect of a stronger expected revenue base in 2004-05 and a significant upward revision to nominal GDP growth in 2005-06.

Relative to MYEFO, nominal GDP growth for 2005-06 has been revised up by 1¾ percentage points to 7½ per cent — despite a slight downward revision to real GDP growth — reflecting significant increases to estimated growth in the GDP deflator as a result of recent increases in commodity export prices (see Box 3 in Statement 3). These increases are expected to lift corporate profits significantly in 2005-06, which — due to the timing of company tax collections — will boost revenue in both 2005-06 and 2006-07. Company tax revenue over the projection years of 2006-07, 2007-08 and 2008-09 reflects a technical assumption that commodity prices return to their long-run average level over the first two years of the projection period (see Box 7 in Statement 3).

Further detail on how the revised outlook for the economy has affected individual revenue heads over the forward estimates period is provided later in this statement. An analysis of the sensitivity of the taxation revenue estimates to changes in the major economic parameters is provided in Statement 2.

Box 1: Changes to the revenue forecasting methodology

In recent years, revenue has grown more strongly than forecast. Two principal factors have contributed to this:

- nominal GDP has grown more strongly than forecast, because of the stronger than expected housing cycle in 2002 and 2003 and stronger than expected growth in the terms of trade in 2003 and 2004; and
- taxation revenue from companies[2], small unincorporated businesses and personal investors has been growing at an unexpectedly faster pace relative to growth in underlying incomes.

As a result of this divergence between actual and forecast revenue, the revenue forecasting methodology has been adjusted. Estimates in this Budget are based on the revised methodology and result in revenue forecasts and projections being more responsive to changes in forecast and projected income. They mostly affect company income tax and gross income tax from other individuals.

Company tax

Revenue from taxes on company profits has been growing significantly faster than the corporate income tax base. Possible reasons for this include:

- the privatisation of major Government Business Enterprises;
- growth in capital gains made by companies;
- the long period of economic expansion, which has reduced the stock of carried-forward losses to offset tax payable;
- more effective compliance activities of the Australian Taxation Office;
- changes in the structure of ownership of shares, combined with changes in the dividend imputation system, which may have affected the incentive for companies to pay tax in Australia in order to maximise franking credits; and
- the increasing tendency for small businesses to incorporate.

Gross other individuals

Revenue from taxes on the incomes of personal investors has been growing strongly owing to strong corporate profits and consequent dividend payments. Revenues on realised capital gains have also been growing strongly because of asset price increases in respect of shares and housing. Income earned by small unincorporated businesses and increasing numbers of self-employed persons is also contributing to this revenue strength.

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2 Strength in company tax revenue growth was highlighted in the 2004-05 Budget (page 5-10).

Other variations

Tax collections to the end of the March quarter 2005 were 8.4 per cent higher than last year, compared with expected growth of 7.6 per cent at MYEFO. The strength in tax collections in the year to date has largely reflected the stronger than expected employment growth during the second half of 2004.

The Budget estimates of tax revenue in 2004-05 factor in a deceleration in collections growth in the final quarter of the year, reflecting an expectation of weakening company tax collections, and lower forecast nominal GDP growth. Company profits are expected to be somewhat weaker than previously forecast for 2004-05, reflecting weaker than expected profits from the private non-financial sector in the second half of 2004.

The Budget estimates also incorporate adjustments to forecasting methodology to align the estimates more closely to recent experience (see Box 1). These adjustments affect the gross other individuals, refunds for individuals and company income tax revenue heads and generally increase estimated revenue since MYEFO for 2005-06 and the projection years.

ESTIMATES OF REVENUE

Total revenue

Total revenue for 2005-06 is expected to increase by $11.8 billion, an increase of 5.8 per cent on estimated revenue in 2004-05. Of this, taxation revenue is expected to increase by $11.1 billion (5.8 per cent) and non-taxation revenue is expected to increase by $779 million (6.3 per cent).

The revenue estimates for 2004-05 and 2005-06 are provided in Table 4. Descriptions of the revenue heads are provided in Appendix B.

Table 4: Australian Government general government revenue

	Estimates		Change on 2004-05	
	2004-05	2005-06		
	$m	$m	$m	%
Income taxation				
Individuals and other withholding				
Gross income tax withholding	97,990	101,140	3,150	3.2
Gross other individuals	23,640	25,440	1,800	7.6
less: Refunds	13,700	15,000	1,300	9.5
Total individuals and other withholding	107,930	111,580	3,650	3.4
Companies	40,610	48,040	7,430	18.3
Superannuation funds				
Contributions and earnings	5,090	5,070	-20	-0.4
Superannuation surcharge	1,290	1,240	-50	-3.9
Total superannuation funds	6,380	6,310	-70	-1.1
Petroleum resource rent tax	1,460	1,350	-110	-7.5
Income taxation revenue	**156,380**	**167,280**	**10,900**	**7.0**
Excise and customs				
Excise duty				
Petroleum and other fuel products	13,620	13,980	360	2.6
Crude oil	650	620	-30	-4.6
Alcohol products	2,460	2,550	90	3.7
Tobacco	5,280	5,340	60	1.1
Total excise duty	22,010	22,490	480	2.2
Customs duty				
Textiles, clothing and footwear	1,000	790	-210	-21.0
Passenger motor vehicles	1,450	1,448	-2	-0.1
Excise-like goods	1,680	1,600	-80	-4.8
Other imports	1,884	1,533	-351	-18.6
less: Refunds and drawbacks	300	300	0	0.0
Total customs duty	5,714	5,071	-643	-11.3
Excise and customs revenue	**27,724**	**27,561**	**-163**	**-0.6**
Indirect taxation				
Wine equalisation tax	690	700	10	1.4
Luxury car tax	300	310	10	3.3
Other taxes	190	220	30	15.8
Indirect taxation revenue	**1,180**	**1,230**	**50**	**4.2**
Other taxation				
Fringe benefits tax(a)	3,050	3,350	300	9.8
Agricultural levies	572	583	11	1.9
Other taxes	1,296	1,264	-32	-2.5
Other taxation revenue	**4,917**	**5,196**	**279**	**5.7**
Taxation revenue	**190,201**	**201,267**	**11,065**	**5.8**
Non-taxation				
Sales of goods and services	4,828	4,965	137	2.8
Dividends	3,146	3,312	166	5.3
Interest received	1,562	2,000	438	28.1
Other	2,929	2,967	38	1.3
Non-taxation revenue	**12,465**	**13,245**	**779**	**6.3**
Total revenue	**202,666**	**214,511**	**11,845**	**5.8**

(a) Consistent with GFS reporting standards, excludes fringe benefits tax collected from Australian Government agencies (estimated at $390 million in 2004-05 and $400 million in 2005-06).

Revenue estimates by revenue head

Income taxation revenue

Individuals and other withholding taxation

Estimated revenue from individuals for 2004-05, 2005-06 and the projection years is provided in Table 5. Revenue from individuals is estimated to increase by $3.7 billion (3.4 per cent) in 2005-06, reflecting the impact of stronger employment and solid growth in the incomes of small unincorporated businesses and personal investors, partly offset by personal tax cuts.

Table 5: Individuals and other withholding taxation revenue

	Actual	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m	$m
Individuals and other withholding						
Gross income tax withholding	90,095	97,990	101,140	106,780	114,300	122,430
Gross other individuals	21,010	23,640	25,440	25,990	27,180	28,960
less: Refunds	12,325	13,700	15,000	15,810	16,580	17,830
Total	**98,779**	**107,930**	**111,580**	**116,960**	**124,900**	**133,560**
Includes Medicare levy(a) revenue of:	*5,560*	*6,000*	*6,360*	*6,690*	*7,030*	*7,390*

(a) Medicare levy for 2003-04 is an estimate.

Gross income tax withholding

Gross income tax withholding revenue is expected to increase by $3.2 billion (3.2 per cent) in 2005-06. The increase reflects the flow on effect of stronger expected revenue in 2004-05 and the impact of stronger estimated employment and slightly stronger wage growth in 2005-06. Personal tax cuts from 1 July 2005 dampen these effects on revenue.

Gross other individuals

Gross revenue from other individuals is expected to increase by $1.8 billion (7.6 per cent) in 2005-06. The increase reflects stronger expected income from dividends and small unincorporated businesses, partly offset by personal tax cuts.

Income tax refunds for individuals

Refunds for individuals are expected to increase by $1.3 billion (9.5 per cent) in 2005-06, reflecting the effect of increases in estimated revenue from gross income tax withholding and from other individuals in 2004-05. Partly offsetting this, a reassessment of the relationship between prior year revenue and current year refunds to better reflect recent outcomes has the effect of reducing refunds and increasing revenue over the forward estimates period.

Medicare levy

Revenue from the Medicare levy is expected to increase by around $360 million (6.0 per cent) in 2005-06. Movements in revenue from the Medicare levy are generally consistent with growth in revenue from personal income taxes.

Companies and other related income taxation

Estimated revenue from companies for 2004-05, 2005-06 and the projection years is provided in Table 6.

Table 6: Companies and other related income taxation revenue

	Actual	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m	$m
Companies	36,337	40,610	48,040	50,140	50,780	52,360
Superannuation funds						
Contributions and earnings	4,487	5,090	5,070	5,380	5,770	6,220
Superannuation surcharge	1,298	1,290	1,240	350	210	270
Total superannuation funds	5,785	6,380	6,310	5,730	5,980	6,490
Petroleum resource rent tax	1,165	1,460	1,350	1,630	1,770	1,520
Total	**43,287**	**48,450**	**55,700**	**57,500**	**58,530**	**60,370**

Company income taxation

Company taxation revenue is expected to increase by $7.4 billion (18.3 per cent) in 2005-06. The increase is largely the result of a stronger outlook for company profits in 2005-06. This mainly reflects the higher export prices that companies have secured for exports of coal and iron ore in the last quarter of 2004-05 and through 2005-06.

Superannuation funds taxation

Taxation revenue from superannuation contributions and earnings income is expected to decrease by $20 million (0.4 per cent) in 2005-06. This decrease reflects the flow-on effect of a lower expected outcome for superannuation contributions and earnings taxation in 2004-05, partly offset by higher expected earnings growth in 2005-06.

Superannuation surcharge

Revenue from the superannuation surcharge is expected to decrease by $50 million (3.9 per cent) in 2005-06, reflecting the reduction in the surcharge rate to 12.5 per cent in 2004-05.

While the abolition of the surcharge from 1 July 2005 will result in zero revenue collected from contributions after that date, allowance has been made for some ongoing revenue from the surcharge over the forward estimates period to recognise liabilities relating to contributions made before 1 July 2005.

Petroleum resource rent tax

Estimated revenue from the petroleum resource rent tax is expected to decrease by $110 million (7.5 per cent) in 2005-06, reflecting lower than expected production of natural gas and crude oil.

Excise and customs revenue

Estimates for 2004-05, 2005-06 and the projection years are provided in Table 7 for excise and customs revenue.

Table 7: Excise and customs revenue

	Actual	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m	$m
Excise duty						
Petroleum and other fuel products						
Petrol	7,423	7,370	7,410	7,500	7,570	7,650
Diesel	5,587	6,100	6,420	6,660	6,910	7,050
Other	210	150	150	110	110	140
Total	13,220	13,620	13,980	14,270	14,590	14,840
Crude oil	309	650	620	580	580	580
Beer	1,633	1,680	1,710	1,740	1,770	1,800
Potable spirits	659	780	840	900	970	1,040
Tobacco	5,247	5,280	5,340	5,360	5,380	5,410
Total excise duty	21,068	22,010	22,490	22,850	23,290	23,670
Customs duty						
Textiles, clothing and footwear	993	1,000	790	840	880	970
Passenger motor vehicles	1,547	1,450	1,448	1,250	1,320	1,430
Excise-like goods	1,581	1,680	1,600	1,600	1,630	1,660
Other imports	1,736	1,884	1,533	1,672	1,792	1,832
less: Refunds and drawbacks	235	300	300	300	300	300
Total customs duty	5,622	5,714	5,071	5,062	5,322	5,592
Total	**26,690**	**27,724**	**27,561**	**27,912**	**28,612**	**29,262**

Excise duty

In 2005-06, revenue from excise duty on petroleum and other fuel products is expected to increase by $360 million (2.6 per cent). The increase results from higher estimated revenue from diesel fuel ($320 million), reflecting an increase in expected activity in agriculture and mining; and from higher estimated revenue from unleaded petrol excise ($40 million), reflecting stronger demand from the energy and transport sectors.

Revenue from crude oil excise is expected to decrease by $30 million (4.6 per cent) in 2005-06, reflecting the effect of a lower expected crude oil price in $A.

Other excise revenue is expected to increase in 2005-06 by $150 million (1.9 per cent), reflecting moderate increases in expected demand for spirits and other alcoholic beverages, with demand for tobacco and beer expected to move in line with population growth.

Customs duty

Customs duty revenue is expected to decrease by $643 million (11.3 per cent) in 2005-06, reflecting the impact of a number of policies designed to increase trade between Australia and the rest of the world. These policies include the measures announced in this Budget, noted above, as well as the impact of tariff reductions for passenger motor vehicles and textiles, clothing and footwear from 1 January 2005, and the effect of the Australia-United States Free Trade Agreement.

Indirect taxation revenue

Revenue estimates for 2004-05, 2005-06 and the projection years are provided in Table 8 for the various categories of sales tax. Information about the goods and services tax can be found in Budget Paper No. 3, *Federal Financial Relations*.

Table 8: Indirect taxation revenue

	Actual	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m	$m
Wine equalisation tax	705	690	700	750	790	840
Luxury car tax	336	300	310	340	360	370
Other	-38	190	220	250	270	290
Total	**1,002**	**1,180**	**1,230**	**1,340**	**1,420**	**1,500**

Revenue from the wine equalisation tax is expected to increase by $10 million (1.4 per cent) in 2005-06, reflecting a slight increase in expected underlying demand.

Revenue from the luxury car tax is expected to increase by $10 million (3.3 per cent) in 2005-06, reflecting underlying demand conditions.

Other taxation revenue

Revenue estimates for fringe benefits tax, agricultural levies and other taxes in 2004-05, 2005-06 and the projection years are provided in Table 9.

Table 9: Other taxation revenue

	Actual	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m	$m
Fringe benefits tax	3,277	3,050	3,350	3,380	3,480	3,580
Agricultural levies	603	572	583	588	580	569
Other levies	73	183	192	148	119	124
Broadcasting licence fees	225	287	264	273	285	298
Other	1,122	825	808	898	872	858
Total	**5,299**	**4,917**	**5,196**	**5,287**	**5,336**	**5,428**

Other taxation revenue is estimated to increase by $279 million (5.7 per cent) in 2005-06, largely reflecting increased estimated revenue from the fringe benefits tax.

Revenue from fringe benefits tax is expected to increase by $300 million (9.8 per cent) in 2005-06, reflecting the effect of slightly higher expected wage growth.

Revenue from agricultural levies, broadcasting licence fees and other levies and taxes for 2005-06 is expected to be largely unchanged from 2004-05 levels.

Non taxation revenue

Revenue estimates for 2004-05 and 2005-06 and the projection years are provided in Table 10 for the various categories of non-taxation revenue.

Table 10: Non-taxation revenue

	Actual	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m	$m
Sales of goods and services	4,314	4,828	4,965	5,194	5,330	5,363
Dividends	4,199	3,146	3,312	2,952	2,357	1,852
Interest received	1,304	1,562	2,000	2,853	3,997	5,025
Other non-taxation revenue	2,684	2,929	2,967	2,884	2,924	2,966
Total	**12,501**	**12,465**	**13,245**	**13,883**	**14,607**	**15,206**

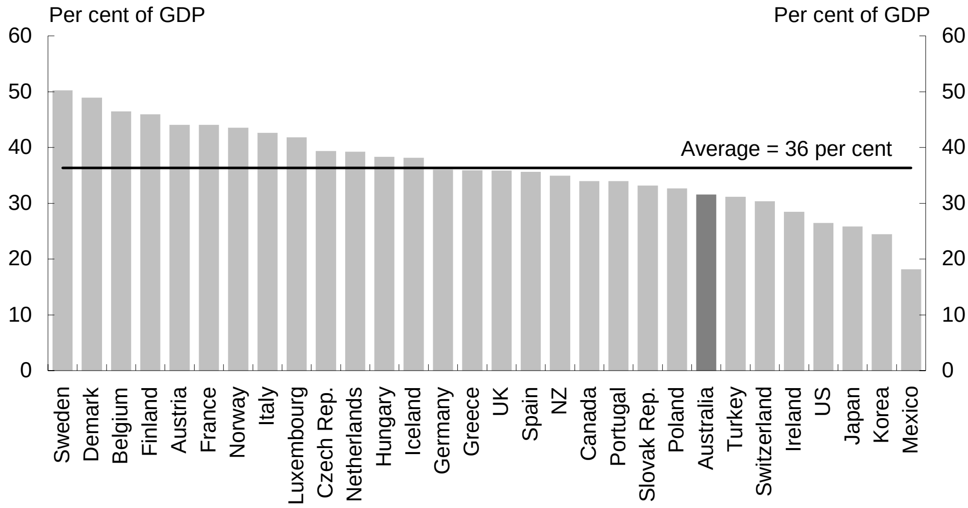
Non-taxation revenue is expected to increase by $779 million (6.3 per cent) in 2005-06, largely reflecting:

- increased interest revenue, largely reflecting higher estimated cash balances — underpinned by strong surpluses in 2004-05 and 2005-06; and
- increased dividends from the Reserve Bank of Australia, largely from higher than expected net interest income, and an increase in realised gains on foreign investments and foreign currency transactions.

APPENDIX A: AUSTRALIA'S TAX SYSTEM

Australia's tax to GDP ratio is the eighth lowest of the 30 OECD countries (Chart A1).

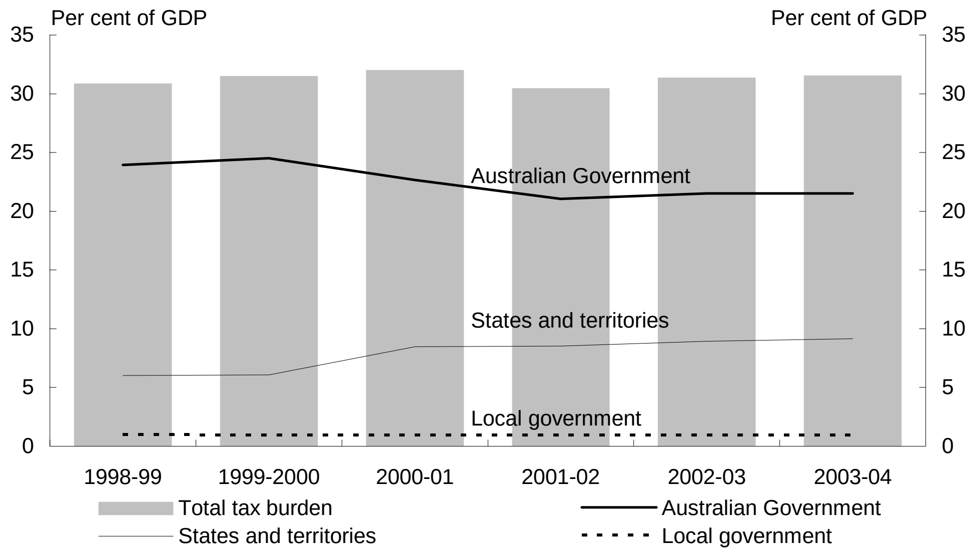
Chart A1: Total tax burden for OECD countries(a)



(a) The OECD's measure of the tax burden is the total taxation revenue of national, state and local governments expressed as a proportion of gross domestic product. For Australia, the data are for the 2002-03 financial year, the latest year where comparable international data are available.
Source: OECD, Revenue Statistics 1965-2003 (2004 Edition).

While the total tax burden for Australia has been relatively steady over recent years, the tax take of the Australian Government has fallen while the tax burden of the states and territories has increased (Chart A2).

Chart A2: Australian tax burden by level of government



The share of tax burden between the Australian Government and the states changed with the introduction of *The New Tax System* in 2000-01. Since then, the tax take of the Australian Government and local governments has been relatively stable, while the tax burden of the states and territories has increased from 8.4 per cent of GDP to 9.1 per cent.

When considering the impact of taxes on Australian households, it is also necessary to take into account the significant increase in assistance going to families from the government, either as offsets to tax or through direct payments.

When this Government came into office in 1996, family assistance totalled around 1.3 per cent of GDP. Since then, the Government has substantially increased the level of assistance provided to families to around 1.7 per cent of GDP in 2004-05, through the introduction of the Family Tax Benefit and the Baby Bonus, and subsequent increases in payments, accompanied by reductions in income test tapers applying to family payments. Elements of this assistance can be accessed through cash payments or reductions in tax.

One way of illustrating the combined effect of cash transfers and tax for families is by showing the change in the real net tax threshold. The net tax threshold is the point at which taxes paid begin to exceed cash transfers received. Table A1 shows that the net tax threshold will have increased by more than 30 per cent in real terms between 1996-97 and 2006-07 for a range of families.

Table A1: Increases in real net tax thresholds for families(a), 1996-97 to 2006-07

Family type (b)	Household wages in 2006-07	Real net tax threshold 1996-97	2006-07	Per cent change
Sole parent (0%)	$0	$34,502	$44,951	30.3
Single income couple with children (100%)	$55,300	$33,931	$44,951	32.5
Dual income couple with children (100 & 33%)	$73,549	$34,559	$47,891	38.6
Dual income couple with children (100 & 67%)	$92,351	$34,657	$46,884	35.3
Dual income couple with children (167 & 100%)	$147,651	$34,641	$47,003	35.7

(a) The net tax threshold is the level of private income at which income tax paid first exceeds cash benefits received. Dollar amounts are calculated in 2005-06 prices.

(b) Families are assumed to have two children — one aged 3 years and the other aged 8 years. The numbers in brackets represent the wages of each working adult in the family, expressed as a proportion of average weekly ordinary time earnings for full-time employees (AWOTE).

APPENDIX B: DESCRIPTION OF THE REVENUE HEADS

Income taxation

Individuals and other withholding taxation

These revenue heads broadly cover all personal income tax. A schedule of the personal income tax rates for the period covered in this Budget is provided in Table B1.

Gross income tax withholding

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 often withheld from companies, rather than individuals, but are not separately identified from other PAYG revenues.

Gross other individuals

Gross 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 investment activities;
- 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 with annual tax liabilities of $8,000 or more and individuals who are registered for the GST will generally make quarterly payments. Individuals who have annual taxation liabilities of less than $8,000 and are not registered for the GST have the choice of making quarterly payments or an annual payment.

Income tax refunds for individuals

A final assessment of the income tax liabilities of individual taxpayers is normally 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. Tax credits typically accrue from PAYG withholding payments deducted by employers from wages and salaries, and from PAYG instalments made by taxpayers through a Business Activity Statement or Income Activity Statement.

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 made after the conclusion of the year to which it relates.

Medicare levy

The Medicare levy forms an integral part of the personal income tax system and, as such, revenue from the Medicare levy is included in the three revenue heads described above.

CORRIGENDUM

Budget Paper No. 1, *Budget Strategy and Outlook 2005-06* — Statement 5

Replace Table B1: Personal Income Tax Rates on page 5-19 with the following table:

Table B1: Personal income tax rates[(a)]

	From 1 July 2003		From 1 July 2004		From 1 July 2005		From 1 July 2006	
	Taxable income	Per cent	Taxable income	Per cent	Taxable income	Per cent	Taxable income	Per cent
Residents	$0–$6,000	Nil	$0–$6,000	Nil	$0–$6,000	Nil	$0–$6,000	Nil
	$6,001–$21,600	17	$6,001–$21,600	17	$6,001–21,600	15	$6,001–21,600	15
	$21,601–$52,000	30	$21,601–$58,000	30	$21,601–$63,000	30	$21,601–$70,000	30
	$52,001–$62,500	42	$58,001–$70,000	42	$63,001–$95,000	42	$70,001–$125,000	42
	> $62,500	47	> $70,000	47	> $95,000	47	> $125,000	47
Non-residents	$0–$21,600	29	$0–$21,600	29	$0–$21,600	29	$0–$21,600	29
	$21,601–$52,000	30	$21,601–$58,000	30	$21,601–$63,000	30	$21,601–$70,000	30
	$52,001–$62,500	42	$58,001–$70,000	42	$63,001–$95,000	42	$70,001–$125,000	42
	> $62,500	47	> $70,000	47	> $95,000	47	> $125,000	47
Medicare levy	$0–$15,529	Nil	$0–$15,902	Nil	$0–$15,902	Nil	$0–$15,902	Nil
for singles(b)	$15,530–$16,788	20% of > $15,529	$15,903–$17,191	20% of > $15,902	$15,903–$17,191	20% of > $15,902	$15,903–$17,191	20% of > $15,902
	> $16,788	1.5	> $17,191	1.5	> $17,191	1.5	> $17,191	1.5

(a) These standard income tax rates can be offset by a range of concessional arrangements, including the senior Australians tax offset, the spouse tax offset, the low income tax offset and the mature age worker tax offset.
(b) These standard Medicare levy rates apply to singles. Different concessional and penalty rates apply in certain circumstances.

Companies and other related income taxation

These revenue heads broadly cover all income taxes paid by corporate type entities. A schedule of the company income tax rates for the period covered in this Budget is provided in Table B2.

Table B2: Company and other related income tax rates

	From 1/7/2003 Per cent	From 1/7/2004 Per cent	From 1/7/2005 Per cent
Companies	30	30	30
Superannuation funds			
Complying funds	15	15	15
Non-complying funds	47	47	47
Superannuation surcharge			
Surcharge rate	14.5	12.5	0
Lower surcharge threshold	$94,691	$99,710	-
Upper surcharge threshold	$114,984	$121,075	-
Petroleum resource rent tax	40	40	40

Company income taxation

Company income tax includes all income taxes paid by companies, including incorporated and unincorporated associations, limited partnerships and some public unit trusts.

Generally, every resident company that derives assessable income (including capital gains), whether sourced within or outside of Australia, and every non-resident company that derives assessable income from Australian sources, is required to pay company tax.

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 able to make an annual payment.

Superannuation funds taxation

Like companies, superannuation funds are taxed through the PAYG instalment system, but generally at a concessional rate of 15 per cent in relation to taxable contributions received, capital gains and investment income. Only two-thirds of a capital gain is included in assessable income if the asset is held for at least 12 months.

Superannuation surcharge

Superannuation surcharge is levied on the surchargeable contributions of a superannuation fund member whose adjusted taxable income exceeds the lower income surcharge threshold in a financial year.

Surchargeable contributions include all employer contributions, certain 'golden handshakes' and tax deductible personal contributions made to superannuation funds. Adjusted taxable income includes fringe benefits and surchargeable contributions.

The rate of surcharge levied phases in from the lower income surcharge threshold to an upper income surcharge threshold. The maximum rate of surcharge until 2002-03 was 15 per cent. This was been reduced to 14.5 per cent for 2003-04 and 12.5 per cent for 2004-05. The surcharge is being abolished for contributions made after 1 July 2005.

Payments are generally received from superannuation funds, but may also be paid by the member as the liability for the surcharge accrues, or if the surchargeable contributions are in the hands of the member at the time the surcharge liability is assessed.

Petroleum resource rent tax

Petroleum resource rent tax is levied on economic 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. The tax is levied at a rate of 40 per cent of a project's economic profit. The amount paid is deductible from a company's total profit when determining its company tax liability.

Excise and customs duty

Excise duty

The major categories of excisable products are petroleum and other fuel products, crude oil, oils and lubricants, 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 kerosene, 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 kerosene 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.

Crude oil excise provides a return to the community for the exploitation of its natural resources. There are two sources of excise on crude oil:

- production from offshore fields in the North-West Shelf production licence areas that are not subject to petroleum resource rent tax; and
- production from onshore fields and fields in coastal waters.

The rate of excise varies according to the quantity of crude oil sold, the sale price of the crude oil, and the dates of discovery and development of the oil field.

Other excise is derived from beer, spirits, other alcoholic beverages (other than wine) and tobacco products.

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

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

Excise indexation

The excise rates for petroleum products and crude oil are not indexed. The rates of duty for other excisable products are adjusted every August and February in line with half yearly CPI movements (Table B3). If the change in the CPI is negative, the excise rate is not reduced but instead the decline is carried forward to be set off against the next positive CPI movement.

Excise indexation for petroleum products was removed in March 2001.

Table B3: Excise rates

Commodity	Rates applying from 1 Aug 2003 $	Rates applying from 2 Feb 2004 $	Rates applying from 2 Aug 2004 $	Rates applying from 1 Feb 2005 $
Petroleum and other fuel products (per litre)				
Unleaded petrol	0.38143	0.38143	0.38143	0.38143
Ultra low sulphur diesel	0.38143	0.38143	0.38143	0.38143
Other diesel	0.39143	0.40143	0.40143	0.40143
Aviation gasoline	0.03114	0.03114	0.03114	0.03114
Aviation kerosene	0.03151	0.03151	0.03151	0.03151
Fuel oil	0.07557	0.07557	0.07557	0.07557
Heating oil and kerosene (for burner use)	0.07557	0.07557	0.07557	0.07557
Fuel ethanol	0.38143	0.38143	0.38143	0.38143
Biodiesel(a)		0.38143	0.38143	0.38143
Greases (per kilogram)	0.05449	0.05449	0.05449	0.05449
Oils and lubricants, excluding greases (per litre)	0.05449	0.05449	0.05449	0.05449
Beer (per litre of alcohol over 1.15 per cent)				
Draught beer, low strength	5.94	6.01	6.09	6.16
Draught beer, mid strength	18.65	18.86	19.12	19.35
Draught beer, high strength	24.40	24.67	25.02	25.32
Other beer, low strength	29.74	30.07	30.49	30.86
Other beer, mid strength	34.66	35.04	35.53	35.96
Other beer, high strength	34.66	35.04	35.53	35.96
Other beverages, not exceeding 10 per cent alcohol content	34.66	35.04	35.53	35.96
Potable spirits (per litre of alcohol)				
Brandy	54.83	55.43	56.21	56.88
Fruit brandy, whisky, rum and liqueurs	58.72	59.37	60.20	60.92
Other spirits, exceeding 10 per cent alcohol content	58.72	59.37	60.20	60.92
Cigarettes, cigars and tobacco (tobacco content of 0.8 grams or less per stick)	0.21804	0.22044	0.22353	0.22621
Tobacco products (per kilogram)	272.55	275.55	279.41	282.76

(a) Biodiesel became subject to excise duty from 18 September 2003.

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 and textile, clothing and footwear are expected to account for around one-third of the total duty collected. A further one-third of customs duty revenue is expected to be derived from duty imposed on imports of petroleum products, tobacco, beer and spirits, which is akin to excise duty on these items. In general, other dutiable goods attract a general tariff rate of five per cent. The Government is removing the three per cent tariff applying to business inputs imported under a Tariff Concession Order from 11 May 2005.

Table B4: Tariff rates

	Applying before 1 January 2005 %	Applying from 1 January 2005 %	Applying from 11 May 2005 %
General tariff	5	5	5
Passenger motor vehicles	15	10	10
Textiles clothing and footwear			
Clothing and finished textiles	25	17.5	17.5
Cotton sheeting, fabric, carpet and footwear	15	10	10
Sleeping bags, table linen and footwear parts	10	7.5	7.5
Tariff concession order			
Consumer goods	0	0	0
Other (business inputs)	3	3	0

Indirect taxation

Wine equalisation tax

All wines, meads, ciders and sakes are subject to a wine equalisation tax of 29 per cent on the wholesale value of the goods. The tax was introduced as part of *The New Tax System* to maintain the level of taxation on cask wine, subsequent to the removal of the previous 41 per cent wholesale sales tax on wine and the application of the goods and services tax.

Unlike alcohol excises, the wine equalisation tax is an *ad valorem* tax. It is calculated at a rate of 29 per cent of the final wholesale price or, in certain other permitted circumstances, of a nominal wholesale value calculated as 50 per cent of the retail price, or alternatively at the average wholesale price for identical wine.

From 1 October 2004, a rebate is payable on the first $290,000 in wine equalisation tax paid annually by any producer.

Luxury car tax

The luxury car tax was implemented on 1 July 2000 as part of *The New Tax System* to maintain the long-standing policy of successive Australian Governments to have a tax differentiation between luxury vehicles and other vehicles sold in Australia.

Its introduction prevented disproportionate falls in the price of luxury vehicles, compared to standard model vehicles at pricing points just below the threshold, when the goods and services tax rate of 10 per cent replaced the previous wholesale sales tax rate of 45 per cent.

The luxury car tax applies at a rate of 25 per cent for every dollar over the luxury car threshold. The current luxury car threshold is $57,009. The threshold is indexed annually using the motor vehicle purchase component of the CPI, which is composed of observed price movements for new vehicles sold in Australia.

Other taxation

Fringe benefits tax

Fringe benefits tax 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.

The tax is payable by employers and is assessed on the value of the fringe benefits provided to employees or their associates. Fringe benefits tax is levied at 48.5 per cent of the grossed-up taxable value of benefits, as calculated under the fringe benefits tax rules.

Instalments are paid by employers (on a Business Activity Statement) for each quarter of the fringe benefits tax year, which runs from April to March. A final balancing payment is due in May, together with the lodgement of a fringe benefits tax return.

Consistent with Government Finance Statistics reporting standards, fringe benefits tax reported at the general government level excludes revenue collected from Australian Government agencies.

Agricultural levies

Agricultural levies and charges are used to fund industry activities, such as research and development, marketing and promotion, residue testing, and animal health programmes.

The need for a levy is usually identified by the industry itself and the levy is generally collected at the first point of sale of the primary produce or point of further processing.

All levies and charges are paid into the Consolidated Revenue Fund without deduction, and then disbursed to fund the relevant programme.

Other levies

The major contributor to this category is a levy of around $80 million, imposed on the coal mining industry under the *Coal Mining Industry (Long Service Leave Funding) Act 1992*. The purpose of the levy is to manage and protect the long service leave entitlements of workers in the industry.

Broadcasting licence fees

Broadcasting licence fees are payable by all commercial radio and television licensees. The licence fees are calculated as a percentage of the licensees' gross earnings for the previous year.

Other taxes

The major contributor to this revenue head is licence fees payable for the operation of radio communications equipment and telecommunications networks used to provide carriage services to the public. These fees total approximately $185 million.

Other contributors include:

- levies totalling approximately $90 million which are collected by the Department of Transport and Regional Services, including Aircraft Noise Levies, the Stevedoring Levy and the Oil Pollution Compensation Fund levy; and
- other fees totalling approximately $59 million, including Interstate Road Transport registration fees, Territory regulatory fees, taxes and fines, Airport leases — in lieu of land tax, *Trade Practices Act 1974* fees, Navigation Act fees and Airport Building Controllers fees.

Non-taxation revenue

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 and territories.

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.

Interest

Interest from other Governments

This category mainly consists of revenue from the states for interest 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 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.

Other sources of non-taxation revenue

Other non-taxation revenue includes petroleum royalties paid by producers operating in the Timor Sea and the North-West Shelf oil and gas fields, Child Support Trust Revenue (collected by the Child Support Agency) and seigniorage from circulation coin production.

APPENDIX C: FORWARD ESTIMATES OF RECEIPTS

Table C1: Australian Government general government receipts (cash basis)

	Actual	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m	$m
Income taxation						
Individuals and other withholding						
Gross income tax withholding	89,638	97,190	100,400	105,850	113,290	121,350
Gross other individuals	19,935	22,400	24,390	24,810	26,070	27,730
less: Refunds	12,325	13,700	15,000	15,810	16,580	17,830
Total individuals and other withholding	97,247	105,890	109,790	114,850	122,780	131,250
Companies	36,101	39,600	47,510	49,260	49,870	51,420
Superannuation funds						
Contributions and earnings	4,502	5,080	5,080	5,360	5,740	6,190
Superannuation surcharge	1,050	1,180	1,150	360	250	310
Total superannuation funds	5,551	6,260	6,230	5,720	5,990	6,500
Petroleum resource rent tax	1,168	1,460	1,350	1,630	1,770	1,520
Income taxation receipts	**140,067**	**153,210**	**164,880**	**171,460**	**180,410**	**190,690**
Excise and customs						
Excise duty						
Petrol	7,434	7,370	7,410	7,500	7,570	7,650
Diesel	5,587	6,100	6,420	6,660	6,910	7,050
Other fuel products	210	150	150	110	110	140
Crude oil	309	650	620	580	580	580
Beer	1,633	1,680	1,710	1,740	1,770	1,800
Potable spirits	659	780	840	900	970	1,040
Tobacco	5,247	5,280	5,340	5,360	5,380	5,410
Total excise duty	21,079	22,010	22,490	22,850	23,290	23,670
Customs duty						
Textiles, clothing and footwear	993	1,000	790	840	880	970
Passenger motor vehicles	960	850	840	650	720	830
Excise-like goods	1,581	1,680	1,600	1,600	1,630	1,660
Other imports	1,739	1,880	1,530	1,670	1,790	1,830
less: Refunds and drawbacks	235	300	300	300	300	300
Total customs duty	5,038	5,110	4,460	4,460	4,720	4,990
Excise and customs receipts	**26,117**	**27,120**	**26,950**	**27,310**	**28,010**	**28,660**
Indirect taxation						
Wine equalisation tax	704	690	700	750	790	840
Luxury car tax	335	300	310	340	360	370
Other taxes	-48	30	50	80	100	120
Indirect taxation receipts	**992**	**1,020**	**1,060**	**1,170**	**1,250**	**1,330**
Other taxation						
Fringe benefits tax	3,226	3,220	3,320	3,400	3,500	3,600
Agricultural levies	603	572	583	588	580	569
Other taxes	1,239	1,063	1,037	1,047	1,032	1,046
Other taxation receipts	**5,068**	**4,855**	**4,939**	**5,035**	**5,111**	**5,215**
Taxation receipts	**172,243**	**186,205**	**197,829**	**204,975**	**214,781**	**225,895**
Non-taxation						
Sales of goods and services	4,422	5,015	5,165	5,385	5,526	5,565
Dividends	3,223	3,808	3,632	2,952	2,357	1,852
Interest received	1,056	1,460	1,828	2,649	3,783	4,789
Other	6,028	6,174	6,061	5,931	6,078	6,144
Non-taxation receipts	**14,729**	**16,457**	**16,686**	**16,917**	**17,744**	**18,350**
Total receipts	**186,971**	**202,662**	**214,515**	**221,891**	**232,525**	**244,245**

APPENDIX D: CHANGES IN REVENUE SINCE MYEFO

Table D1: Reconciliation of 2004-05 general government revenue (accrual basis)

	MYEFO	Budget	Change on MYEFO	
	$m	$m	$m	%
Income taxation				
Individuals and other withholding				
Gross income tax withholding	96,550	97,990	1,440	1.5
Gross other individuals	22,210	23,640	1,430	6.4
less: Refunds	13,700	13,700	0	0.0
Total individuals and other withholding	105,060	107,930	2,870	2.7
Companies	40,870	40,610	-260	-0.6
Superannuation funds				
Contributions and earnings	5,390	5,090	-300	-5.6
Superannuation surcharge	1,320	1,290	-30	-2.3
Total superannuation funds	6,710	6,380	-330	-4.9
Petroleum resource rent tax	1,560	1,460	-100	-6.4
Income taxation revenue	**154,200**	**156,380**	**2,180**	**1.4**
Excise and customs				
Excise duty				
Petrol	7,350	7,370	20	0.3
Diesel	5,900	6,100	200	3.4
Other fuel products	150	150	0	0.0
Crude oil	550	650	100	18.2
Beer	1,660	1,680	20	1.2
Potable spirits	780	780	0	0.0
Tobacco	5,260	5,280	20	0.4
Total excise duty	21,650	22,010	360	1.7
Customs duty				
Textiles, clothing and footwear	870	1,000	130	14.9
Passenger motor vehicles	1,354	1,450	96	7.1
Excise-like goods	1,610	1,680	70	4.3
Other imports	2,110	1,884	-226	-10.7
less: Refunds and drawbacks	230	300	70	30.4
Total customs duty	5,714	5,714	0	0.0
Excise and customs revenue	**27,364**	**27,724**	**360**	**1.3**
Indirect taxation				
Wine equalisation tax	690	690	0	0.0
Luxury car tax	330	300	-30	-9.1
Other taxes	120	190	70	58.3
Indirect taxation revenue	**28,504**	**28,904**	**400**	**1.4**
Other taxation				
Fringe benefits tax	3,020	3,050	30	1.0
Agricultural levies	575	572	-3	-0.6
Other levies	95	183	88	93.0
Broadcasting licence fees	234	287	53	22.6
Other taxes	994	825	-168	-16.9
Other taxation revenue	**4,918**	**4,917**	**0**	**0.0**
Taxation revenue	**187,622**	**190,201**	**2,580**	**1.4**
Non-taxation				
Sales of goods and services	4,404	4,828	424	9.6
Dividends	3,050	3,146	96	3.1
Interest received	1,435	1,562	127	8.8
Other	2,932	2,929	-3	-0.1
Non-taxation revenue	**11,821**	**12,465**	**644**	**5.4**
Total revenue	**199,443**	**202,666**	**3,223**	**1.6**

Table D2: Reconciliation of 2005-06 general government revenue (accrual basis)

	MYEFO	Budget	Change on MYEFO	
	$m	$m	$m	%
Income taxation				
Individuals and other withholding				
Gross income tax withholding	102,210	101,140	-1,070	-1.0
Gross other individuals	23,030	25,440	2,410	10.5
less: Refunds	15,020	15,000	-20	-0.1
Total individuals and other withholding	110,220	111,580	1,360	1.2
Companies	43,360	48,040	4,680	10.8
Superannuation funds				
Contributions and earnings	5,380	5,070	-310	-5.8
Superannuation surcharge	1,200	1,240	40	3.3
Total superannuation funds	6,580	6,310	-270	-4.1
Petroleum resource rent tax	1,460	1,350	-110	-7.5
Income taxation revenue	**161,620**	**167,280**	**5,660**	**3.5**
Excise and customs				
Excise duty				
Petrol	7,370	7,410	40	0.5
Diesel	6,130	6,420	290	4.7
Other fuel products	150	150	0	0
Crude oil	510	620	110	21.6
Beer	1,690	1,710	20	1.2
Potable spirits	870	840	-30	-3.4
Tobacco	5,270	5,340	70	1.3
Total excise duty	21,990	22,490	500	2.3
Customs duty				
Textiles, clothing and footwear	660	790	130	19.7
Passenger motor vehicles	1,350	1,448	98	7.3
Excise-like goods	1,530	1,600	70	4.6
Other imports	2,040	1,533	-507	-24.9
less: Refunds and drawbacks	230	300	70	30.4
Total customs duty	5,350	5,071	-279	-5.2
Excise and customs revenue	**27,340**	**27,561**	**221**	**0.8**
Indirect taxation				
Wine equalisation tax	695	700	5	0.7
Luxury car tax	345	310	-35	-10.1
Other taxes	170	220	50	29.4
Indirect taxation revenue	**28,550**	**28,791**	**241**	**0.8**
Other taxation				
Fringe benefits tax	3,260	3,350	90	2.8
Agricultural levies	588	583	-6	-0.9
Other levies	102	192	90	88.2
Broadcasting licence fees	243	264	21	8.6
Other taxes	1,064	808	-256	-24.1
Other taxation revenue	**5,257**	**5,196**	**-61**	**-1.2**
Taxation revenue	**195,427**	**201,267**	**5,840**	**3.0**
Non-taxation				
Sales of goods and services	4,491	4,965	474	10.6
Dividends	3,076	3,312	236	7.7
Interest received	1,602	2,000	399	24.9
Other	2,903	2,967	65	2.2
Non-taxation revenue	**12,071**	**13,245**	**1,174**	**9.7**
Total revenue	**207,497**	**214,511**	**7,014**	**3.4**

APPENDIX E: ACCRUAL AND CASH TAXATION ESTIMATES

Table E1: Estimates of taxation revenue on an accrual and cash basis

	2004-05 $b	2005-06 $b	2006-07 $b	2007-08 $b	2008-09 $b
Tax revenue (accrual)	190.2	201.3	209.0	218.8	230.1
Tax receipts (cash)	186.2	197.8	205.0	214.8	225.9
Difference (accrual less cash)	**4.0**	**3.4**	**4.0**	**4.0**	**4.2**
Memorandum items:					
Deferred company tax payments	-0.3	-0.3	0.0	0.0	0.0
ACIS(a)	0.6	0.6	0.6	0.6	0.6
Other	3.7	3.2	3.4	3.4	3.6
Total	4.0	3.4	4.0	4.0	4.2

(a) Automotive Competitiveness and Investment Scheme.

Accrual estimates are prepared using the tax liability method of revenue recognition. Under the tax liability method, 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 relevant authority. 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 set off against 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 $615 million of the difference between the accrual and cash estimates in 2005-06.

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 five 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 five year period.

The impact of these deferred payments has been to increase the cash taxation receipt estimates by around $325 million in 2004-05 and $330 million in 2005-06, while they have no impact on the accrual estimates in either year.

Other

This category consists of other 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 F: TAX EXPENDITURES

This appendix contains an overview of the cost of tax expenditures provided to taxpayers through the tax system.

Tax expenditures provide a benefit to a specified activity or class of taxpayer. They can be delivered as a tax exemption, tax deduction, tax offset, reduced tax rate or deferral of a tax liability. The Government can use tax expenditures 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 concessions are generally called tax expenditures.

The data reported in this appendix are consistent with tax expenditure data reported in the *2004 Tax Expenditures Statement* published in January 2005. Several considerations need to be taken into account when analysing tax expenditure data (see section 2.1 of the *2004 Tax Expenditures Statement* for a detailed description).

Table F1 contains estimates of total tax expenditures for the period 2001-02 to 2008-09.

Table F1: Aggregate tax expenditures

Year	Superannuation $m	Other tax expenditures $m	Net value of tax expenditures $m	Tax expenditures as a proportion of GDP %
2001-02 (est)	9,860	19,866	29,726	4.2
2002-03 (est)	10,990	19,534	30,524	4.0
2003-04 (est)	12,030	19,178	31,208	3.8
2004-05 (proj)	13,290	19,374	32,664	3.8
2005-06 (proj)	14,580	19,936	34,516	3.7
2006-07 (proj)	15,580	21,507	37,087	3.8
2007-08 (proj)	16,530	22,146	38,676	3.8
2008-09 (prelim)	17,560	22,773	40,333	3.8

Tax expenditures are projected to decline as a proportion of GDP from 4.2 per cent in 2001-02 to around 3.8 per cent in 2008-09. The largest single contributing factor to the decline in tax expenditures is the removal of accelerated depreciation under *The New Business Tax System*.

Table F2 is a list of the major tax expenditures in 2003-04.

Table F2: Major tax expenditures 2004-05

	$m
Large positive tax expenditures	
Concessional taxation of funded superannuation	12,760
Exemption of Family Tax Benefit, Parts A and B, including expense equivalent	2,730
Capital gains tax discount for individuals and trusts	2,580
Senior Australians' Tax Offset	1,680
Tax offset for recipients of certain social security benefits, pensions or allowances	1,100
Exemption of certain income support benefits, pensions or allowances	1,100
Application of statutory formula to value car benefits	1,100
Exemption from excise for 'alternative fuels'	800
Concessional treatment of non-superannuation termination benefits	780
Exemption of 30 per cent private health insurance refund, including expense equivalent	750
Concessional rate of excise levied on aviation gasoline and aviation kerosene	745
Tax offset for low income earners	680
Large negative tax expenditures	
Higher rate of excise levied on cigarettes with less than 0.8 grams of tobacco	-1,380
Accelerated depreciation allowance for plant and equipment	-850

APPENDIX G: RECEIPTS HISTORY AND FORECASTS

Table G1: Australian Government receipts (cash basis)(a)

	1994-95	1995-96	1996-97	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05(est)	2005-06(est)
	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m
Income taxation												
Individuals and other withholding												
Income tax withholding	54,000	59,970	64,521	69,366	75,170	81,055	75,009	78,983	84,134	89,638	97,190	100,400
Other individuals	9,481	10,078	11,820	12,119	13,103	13,370	13,226	16,290	17,436	19,935	22,400	24,390
less: Refunds	7,931	8,285	8,808	9,525	10,325	10,946	10,989	10,637	11,651	12,325	13,700	15,000
Total individuals and other withholding	55,551	61,763	67,533	71,959	77,948	83,478	77,246	84,636	89,919	97,247	105,890	109,790
Companies	15,588	18,252	19,173	19,406	20,734	24,453	31,582	27,230	32,752	36,101	39,600	47,510
Superannuation funds												
Contributions and earnings	1,913	1,634	2,595	2,746	3,630	3,243	4,110	3,550	3,865	4,502	5,080	5,080
Superannuation surcharge				347	286	577	690	824	975	1,050	1,180	1,150
Total superannuation funds	1,913	1,634	2,595	3,093	3,916	3,820	4,800	4,373	4,840	5,551	6,260	6,230
Petroleum resource rent tax	865	791	1,308	907	419	1,184	2,379	1,361	1,712	1,168	1,460	1,350
Income taxation receipts	**73,916**	**82,440**	**90,610**	**95,366**	**103,017**	**112,936**	**116,006**	**117,601**	**129,222**	**140,067**	**153,210**	**164,880**
Excise and customs												
Excise duty												
Petroleum and other fuel products	9,406	10,224	10,543	10,895	10,974	11,189	11,919	12,386	12,866	13,231	13,620	13,980
Crude oil	27	13	9	16	31	219	526	393	417	309	650	620
Other excise	2,567	2,612	2,739	2,663	2,614	2,670	6,572	6,837	7,450	7,539	7,740	7,890
Total excise duty	12,001	12,849	13,291	13,574	13,619	14,078	19,017	19,616	20,733	21,079	22,010	22,490
Customs duty	3,474	3,124	3,289	3,637	3,634	3,771	4,584	4,625	4,982	5,038	5,110	4,460
Excise and customs receipts	**15,475**	**15,973**	**16,580**	**17,211**	**17,253**	**17,849**	**23,601**	**24,241**	**25,715**	**26,117**	**27,120**	**26,950**
Indirect taxation												
Wine equalisation tax							524	640	669	704	690	700
Luxury car tax							171	220	261	335	300	310
Other taxes	11,624	12,955	13,308	14,085	15,162	15,532	1,234	-75	-72	-48	30	50
Indirect taxation receipts	**11,624**	**12,955**	**13,308**	**14,085**	**15,162**	**15,532**	**1,929**	**785**	**858**	**992**	**1,020**	**1,060**

Table G1: Australian Government receipts (cash basis)(a) (continued)

	1994-95	1995-96	1996-97	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05(est)	2005-06(est)
	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m
Other taxation												
Fringe benefits tax	2,740	3,031	3,163	3,168	3,289	3,373	3,207	3,272	3,103	3,226	3,220	3,320
Other taxes	1,933	1,988	2,154	2,390	2,383	1,005	1,312	1,645	1,762	1,842	1,635	1,619
Taxation receipts	**105,687**	**116,386**	**125,815**	**132,219**	**141,104**	**150,695**	**146,056**	**147,544**	**160,661**	**172,243**	**186,205**	**197,829**
Non-taxation												
Interest received	1,790	1,403	1,126	1,139	682	995	1,140	918	982	1,056	1,460	1,828
Dividends and other	2,952	3,899	4,089	3,610	4,659	14,138	13,651	14,080	14,504	13,673	14,997	14,858
Non-taxation receipts	**4,743**	**5,302**	**5,216**	**4,749**	**5,341**	**15,133**	**14,791**	**14,998**	**15,487**	**14,729**	**16,457**	**16,686**
Total receipts	**110,430**	**121,688**	**131,031**	**136,968**	**146,444**	**165,828**	**160,847**	**162,542**	**176,147**	**186,971**	**202,662**	**214,515**

(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.

Table G2: Major categories of receipts as a proportion of gross domestic product (cash basis)(a)

	Taxation receipts														Non-taxation receipts			
	Income tax								Other taxation receipts									
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding	Companies	Super funds	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	FBT	Total other tax	Total tax receipts	Interest	Dividends and other	Total non-tax receipts	Total receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
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	12.1	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	10.8	1.9	1.6	11.5	2.8	0.3	0.2	14.9	1.9	0.5	0.7	0.3	6.2	21.1	0.5	1.0	1.5	22.6
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	6.8	22.5	0.4	0.6	1.0	23.5
1995-96	11.5	2.0	1.7	12.3	3.6	0.3	0.2	16.4	2.0	0.5	0.6	0.6	6.8	23.2	0.3	0.8	1.1	24.3
1996-97	11.8	2.2	1.7	12.8	3.6	0.5	0.2	17.2	2.0	0.5	0.6	0.6	6.7	23.8	0.2	0.8	1.0	24.8

Table G2: Major categories of receipts as a proportion of gross domestic product (cash basis)(a) (continued)

	Taxation receipts														Non-taxation receipts			
	Income tax								Other taxation receipts									
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding	Companies	Super funds	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	FBT	Total other tax	Total tax receipts	Interest	Dividends and other	Total non-tax receipts	Total receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
1997-98	12.0	2.2	1.7	12.9	3.5	0.6	0.2	17.1	2.0	0.5	0.7	0.6	6.6	23.6	0.2	0.6	0.8	24.5
1998-99	12.3	2.2	1.8	13.2	3.5	0.7	0.1	17.5	1.9	0.4	0.6	0.6	6.5	23.9	0.1	0.8	0.9	24.8
1999-00	12.5	2.1	1.8	13.4	3.9	0.6	0.2	18.1	1.8	0.4	0.6	0.5	6.1	24.2	0.2	2.3	2.4	26.6
2000-01	11.2	2.0	1.6	11.6	4.7	0.7	0.4	17.4	1.9	1.0	0.7	0.5	4.5	21.9	0.2	2.0	2.2	24.1
2001-02	11.1	2.3	1.5	11.9	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	11.1	2.3	1.5	11.9	4.3	0.6	0.2	17.0	1.8	1.0	0.7	0.4	4.1	21.2	0.1	1.9	2.0	23.2
2003-04	11.0	2.4	1.5	12.0	4.4	0.7	0.1	17.2	1.7	0.9	0.6	0.4	4.0	21.2	0.1	1.7	1.8	23.0
2004-05(est)	11.3	2.6	1.6	12.3	4.6	0.7	0.2	17.8	1.7	0.9	0.6	0.4	3.8	21.6	0.2	1.7	1.9	23.5
2005-06(est)	10.8	2.6	1.6	11.8	5.1	0.7	0.1	17.8	1.6	0.9	0.5	0.4	3.6	21.3	0.2	1.6	1.8	23.1

(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.

Table G3: Major categories of receipts as a proportion of total receipts (cash basis)(a)

	Taxation receipts														Non-taxation receipts		
	Income tax								Other taxation receipts								
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding	Companies	Super funds	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	FBT	Total other tax	Total tax receipts	Interest	Dividends and other	Total non-tax receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
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 G3: Major categories of receipts as a proportion of total receipts (cash basis)(a) (continued)

	Taxation receipts														Non-taxation receipts		
	Income tax								Other taxation receipts								
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding	Companies	Super funds	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	FBT	Total other tax	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	47.9	10.7	6.6	52.0	19.3	3.0	0.6	74.9	7.2	4.0	2.7	1.7	17.2	92.1	0.6	7.3	7.9
2004-05(est)	48.0	11.1	6.8	52.2	19.5	3.1	0.7	75.6	7.0	3.8	2.5	1.6	16.3	91.9	0.7	7.4	8.1
2005-06(est)	46.8	11.4	7.0	51.2	22.1	2.9	0.6	76.9	6.8	3.7	2.1	1.5	15.4	92.2	0.9	6.9	7.8

(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.

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 while 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 22.6 per cent of gross domestic product (GDP) in 2004-05 to 22.2 per cent of GDP in 2005-06 and then rise slightly to 22.3 per cent of GDP in 2008-09;
- in 2005-06, the social security and welfare, health, education and defence functions together account for approximately 76 per cent of total expenses with social security and welfare itself accounting for approximately 42 per cent of total expenses;
- in real terms, the strongest growth across the Budget and forward estimates years is occurring in the health, education, social security and welfare and defence functions, with other functions either being stable or declining; and
- net capital investment in 2005-06 largely reflects increased investment in the Department of Finance and Administration's construction and refurbishment projects, and the purchase of land and security upgrade of various overseas missions by the Department of Foreign Affairs.

CONTENTS

STATEMENT 6: EXPENSES AND NET CAPITAL INVESTMENT

OVERVIEW

Australian Government general government expenses are expected to grow in real terms in 2005-06 and over the forward estimates period to 2008-09 (Table 1). Expenses as a proportion of gross domestic product (GDP) are forecast to fall slightly over the next four years, from 22.6 per cent of GDP in 2004-05 to 22.3 per cent of GDP in 2008-09.

Table 1: Estimates of expenses

	2004-05		2005-06	2006-07	2007-08	2008-09
	MYEFO(a)	Revised	Estimate	Projections		
Total expenses ($b)	**193.8**	**195.0**	**206.1**	**214.8**	**225.4**	**236.6**
Real growth on previous year(%)(b)	2.9	3.5	1.2	3.5	4.2	3.0
Per cent of GDP	22.4	22.6	22.2	22.2	22.4	22.3

(a) As published in the Mid-Year Economic and Fiscal Outlook 2004-05.
(b) Real growth is calculated using the non-farm gross domestic product (GDP) deflator.

GENERAL GOVERNMENT EXPENSES

Reconciliation of expenses since the 2004-05 Budget

Table 2 provides a reconciliation of expense estimates between the 2004-05 Budget, *Mid-Year Economic and Fiscal Outlook 2004-05* (MYEFO) and the 2005-06 Budget, showing the effect of policy decisions and economic parameter and other variations.

Table 2: Reconciliation of expense estimates

	Estimates		Projections	
	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m
2004-05 Budget expenses	**192,306**	**200,626**	**210,033**	**220,939**
Changes between 2004-05 Budget and MYEFO				
Effect of policy decisions(a)	1,646	2,943	3,250	3,367
Effect of economic parameter variations				
Unemployment benefits	-106	-27	-9	-38
Prices and wages	95	-472	-149	-257
Interest and exchange rates	15	-21	-25	-19
Total economic parameter variations	*4*	*-519*	*-183*	*-314*
Public debt interest	-15	-5	-54	-118
Programme specific parameter variations	-1,500	-1,043	-1,096	-1,068
Slippage in 2004-05 Budget decisions	7	0	0	0
Other variations	1,361	1,583	414	84
Total variations	**1,503**	**2,960**	**2,330**	**1,951**
2004-05 MYEFO expenses	**193,808**	**203,585**	**212,363**	**222,890**
Changes between MYEFO and 2005-06 Budget				
Effect of policy decisions(a)	932	2,040	3,041	3,201
Effect of economic parameter variations				
Unemployment benefits	-59	-370	-331	-364
Prices and wages	57	1,046	455	329
Interest and exchange rates	-6	-30	-60	-67
Total economic parameter variations	*-8*	*646*	*64*	*-102*
Public debt interest	9	30	42	56
Programme specific parameter variations	178	407	394	399
Slippage in 2004-05 Budget decisions	-1	1	0	0
Other variations	94	-628	-1,098	-1,043
Total variations	**1,203**	**2,496**	**2,443**	**2,511**
2005-06 Budget expenses	**195,012**	**206,081**	**214,806**	**225,400**

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

Discussion of the major changes between the 2004-05 MYEFO and the 2005-06 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 2005-06*.

Expense estimates by function

Table 3 sets out the estimates of Australian Government general government expenses by function for the period 2004-05 to 2008-09.

Table 3: Estimates of expenses by function

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
General public services(a)	12,748	12,799	13,067	13,339	13,368
Defence	14,190	15,600	15,851	16,791	17,238
Public order and safety	2,490	2,721	2,792	2,860	2,892
Education	14,533	15,729	16,541	17,336	17,905
Health(a)	35,541	37,544	39,041	40,937	42,812
Social security and welfare(a)	83,814	87,564	92,138	95,943	99,789
Housing and community amenities	1,887	1,968	2,003	1,992	1,894
Recreation and culture(a)	2,473	2,670	2,575	2,563	2,472
Fuel and energy	3,871	4,212	4,198	4,340	4,848
Agriculture, forestry and fishing	2,263	2,520	2,571	2,408	1,622
Mining, manufacturing and construction	1,754	1,916	1,820	1,802	1,833
Transport and communication	2,723	2,806	2,972	3,042	2,879
Other economic affairs	4,782	4,782	4,923	5,100	5,013
Other purposes	11,943	13,250	14,314	16,948	22,002
Total expenses	**195,012**	**206,081**	**214,806**	**225,400**	**236,568**

(a) There has been some reclassification of expenditure that was previously reported under the Aboriginal advancement nec sub-function (social security and welfare) to other primary functions.

Major movements within the estimates of expenses by function between 2004-05 and 2005-06, and across the forward estimates, include increases in the following functions:

- **Defence** due to continued funding increases associated with the Government's White Paper *Defence 2000 — Our Future Defence Force*, together with funding for major Australian Defence Force deployments, such as the operations in Iraq;
- **Education** due to increased schools funding associated with the election commitment School infrastructure — investing in our schools together with increased higher education funding reflecting the majority of the *Our Universities* measures;
- **Health** due to a continued 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 *Welfare to Work* package as well as the continued effect of indexation of payments together with the demographic and social factors that affect demand driven programmes.

Estimates presented in Table 3 above are explained in greater detail for each individual function in the following pages.

General public services

Table 4: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Legislative and executive affairs	850	788	826	941	787
Financial and fiscal affairs	3,730	3,685	3,864	3,763	3,798
Foreign affairs and economic aid(a)	2,936	3,063	2,885	3,041	3,138
General research	2,206	2,324	2,455	2,512	2,509
General services	539	576	629	648	657
Government superannuation benefits	2,487	2,363	2,409	2,434	2,479
Total general public services(b)	**12,748**	**12,799**	**13,067**	**13,339**	**13,368**

(a) In order to better reflect the Australian Federal Police's role in overseas development and assistance missions (such as the Regional Assistance Mission to the Solomon Islands), approximately a third of its departmental funding has been reclassified from the other public order and safety sub-function (public order and safety) to the foreign affairs and economic aid sub-function (general public services).

(b) There has been some reclassification of expenditure that was previously reported under the Aboriginal advancement nec sub-function (social security and welfare) to other primary functions.

Nature of expenses and major trends

The general public services function includes expenses relating to the organisation and operation of government. This includes: expenses related to the Parliament, Governor-General and conduct of elections; expenses related to the collection of taxes, and management of public funds and public debt; and assistance to developing countries including assistance initiatives in the Pacific, contributions to international organisations and the operations of the foreign service. It also includes: expenses related to research in areas not otherwise connected with a specific function; expenses related to overall economic and statistical services and government superannuation benefits (excluding nominal interest expenses on unfunded liabilities which are included under the nominal superannuation interest sub-function in the other purposes function).

Expenses within the function tend to fluctuate over the budget and forward estimates period partly due to one-off factors such as the preparation for a federal election in 2007-08 (legislative and executive affairs sub-function) and the 2006 Census (financial and fiscal affairs sub-function).

General research sub-function expenses are expected to 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 announced in May 2004. Fluctuations in the foreign affairs and economic aid sub-function over the Budget and forward years are due to timing effects in Australia's contributions to multilateral development banks. The increase in expenses in 2008-09 for this sub-function is due to the impact of the Government's decision to write off a proportion of Iraq's debt to Australia.

Defence

Table 5: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Defence	14,190	15,600	15,851	16,791	17,238
Total defence	**14,190**	**15,600**	**15,851**	**16,791**	**17,238**

Nature of expenses and major trends

Expenses in this function are within the Defence portfolio and support operations and 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 over $1.6 billion over the period 2005-06 to 2008-09.

The growth and pattern of expenditure 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, such as the operations in Iraq.

The remaining growth in expenses is largely due to changes in price together with additional funding provided in this and previous budgets for North West Shelf surveillance, logistics, military personnel costs and initiatives, and maintenance of the Defence estate.

Public order and safety

Table 6: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Courts and legal services	663	716	772	824	832
Other public order and safety(a)	1,828	2,005	2,020	2,036	2,061
Total public order and safety	**2,490**	**2,721**	**2,792**	**2,860**	**2,892**

(a) In order to better reflect the Australian Federal Police's role in overseas development and assistance missions (such as the Regional Assistance Mission to the Solomon Islands), approximately a third of its departmental funding has been reclassified from the other public order and safety sub-function (public order and safety) to the foreign affairs and economic aid sub-function (general public services).

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 the courts and legal services sub-function increase from 2004-05 to 2007-08 reflecting the new family law system. The increase in expenditure from 2004-05 to 2005-06 for the other public order and safety sub-function is a result of new protective security and regional counter-terrorism measures.

Education

Table 7: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Higher education	4,735	5,164	5,353	5,528	5,660
Vocational and other education	1,425	1,571	1,590	1,612	1,635
Non-government schools	5,091	5,508	5,916	6,338	6,670
Government schools	2,595	2,851	3,023	3,181	3,234
Schools	*7,686*	*8,359*	*8,939*	*9,519*	*9,904*
Student assistance	569	530	547	569	598
General administration	1	1	1	1	1
School education - specific funding	118	105	111	107	107
Total education	**14,533**	**15,729**	**16,541**	**17,336**	**17,905**

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 10.1 per cent in real terms over the three forward years, 2006-07 to 2008-09, or 3.3 per cent annually on average, with expenses on higher education and schools being the main drivers.

Growth in the higher education sub-function from 2004-05 to 2005-06 reflects the impact of the majority of the *Our Universities* package effective 1 January 2005. Funding associated with *Our Universities* continues to grow over the forward years, along with increases in funding under the Commonwealth Grant Scheme, increases to the number of higher education student places and scholarships and additional funding for capital projects. Growth is also due to the application of the higher education indexation factor.

Growth in expenses relating to schools is driven by funding provided under the *Schools Assistance Act 2004* (the Act). Estimated Australian Government funding of $33 billion, including expenses for the election commitment *$1 billion Investment In Our School Infrastructure*, will be provided to and through the states and territories over the four year period 2005 to 2008 (calendar year) under the Act.

The student assistance sub-function will decline between 2004-05 and 2005-06 as a result of the closure of the Student Financial Supplementation Scheme to new borrowers.

Health

Table 8: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Medical services and benefits(a)	14,672	15,688	16,053	16,530	17,067
Hospital services	1,663	1,808	1,951	2,108	2,272
Health care agreements	8,008	8,407	8,852	9,310	9,478
Hospital services and health care agreements	*9,671*	*10,214*	*10,803*	*11,418*	*11,750*
Pharmaceutical services and benefits	7,214	7,536	8,025	8,735	9,615
Aboriginal and Torres Strait Islander health	312	374	363	381	408
Health services	1,218	1,211	1,207	1,195	1,170
Other health services	1,566	1,621	1,687	1,752	1,843
Other health services	*2,784*	*2,832*	*2,895*	*2,947*	*3,013*
General administration	633	655	654	669	687
Health assistance to the aged	254	244	249	257	272
Total health(b)	**35,541**	**37,544**	**39,041**	**40,937**	**42,812**

(a) The financial impact of premium growth on the forward estimates for the Private Health Insurance Rebate has been allocated to the contingency reserve.

(b) There has been some reclassification of expenditure that was previously reported under the Aboriginal advancement nec sub-function (social security and welfare) to other primary functions.

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).

The major purpose of health function expenditure is to ensure that all Australians have access to essential health services through a range of providers and without excessive price barriers.

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 expected to remain at around 4 per cent of GDP over the Budget and forward estimates years.

Total expenses for this function are estimated to increase by 10.3 per cent in real terms over the three forward years, or on average by around 3.3 per cent per annum. This growth is most pronounced in the areas of hospital services and pharmaceutical services and benefits.

Medical services and benefits funded through Medicare and the Private Health Insurance Rebate are the main contributors to health function expenses, making up around 40 per cent of total health expenditure.

The hospital services sub-function has average annual growth in real terms of 6.0 per cent due to an ageing and increasingly frail veteran community requiring more hospital services.

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 current agreements that cover the period 1 July 2003 to 30 June 2008.

The expense for the pharmaceutical services and benefits sub-function is one of the fastest growing health expenses and is forecast to grow at an average of 5.4 per cent per annum in real terms. This growth is driven by a combination of an ageing population and demand for newer and more expensive drugs.

Box 6.1: Pharmaceutical services and benefits

Table 8.1: Trends in major components of the pharmaceutical services and benefits sub-function

	2004-05	**2005-06**	2006-07	2007-08	2008-09
	$m	**$m**	$m	$m	$m
Pharmaceutical Benefits (Concessional)(a)	4,302	**4,644**	4,993	5,480	6,078
Pharmaceutical Benefits (General)(a)	1,073	**1,130**	1,171	1,297	1,442
Repatriation Pharmaceutical Benefits Scheme(b)	480	**507**	546	595	642
Highly Specialised Drugs(a)	464	**521**	572	628	684
Other(c)	712	**560**	570	560	592
Sub-total Administered Items	7,031	7,362	7,852	8,560	9,438
Departmental Expenses(d)	183	**174**	173	175	177
Total	**7,214**	**7,536**	**8,025**	**8,735**	**9,615**

(a) For a detailed discussion of the Pharmaceutical Benefits Scheme, refer to Outcome 2 of *Health and Ageing Portfolio Budget Statements 2005-06*.
(b) Veterans' Pharmaceutical Services are covered under Outcome 2 of the *Department of Veterans' Affairs (Defence Portfolio) Portfolio Budget Statements 2005-06*.
(c) Subsumed within Outcomes 1 and 2 of *Health and Ageing Portfolio Budget Statements 2005-06*. The decrease in 'Other' in 2005-06 is attributable to the fulfilment of prevalence cohort immunisations for the Meningococcal C Vaccination Programme.
(d) Approximately 20 per cent of Health Insurance Commission departmental expenses and 14 per cent of Health and Ageing departmental expenses are allocated to this sub-function.

Social security and welfare

Table 9: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Assistance to the aged	28,220	29,876	31,656	33,483	35,310
Assistance to veterans and dependents	6,017	6,136	6,185	6,220	6,216
Assistance to people with disabilities	11,658	12,308	12,829	13,454	14,207
Assistance to families with children	25,458	26,691	27,995	28,584	29,307
Assistance to the unemployed	5,181	5,041	5,676	6,164	6,509
Assistance to the sick	87	88	87	86	77
Assistance to the unemployed and sick	*5,269*	*5,129*	*5,763*	*6,250*	*6,586*
Common youth allowance	2,219	2,347	2,487	2,545	2,618
Other welfare programmes	1,273	1,355	1,422	1,483	1,535
Aboriginal advancement nec(a)	1,367	1,419	1,452	1,478	1,510
General administration	2,333	2,302	2,349	2,447	2,499
Total social security and welfare	**83,814**	**87,564**	**92,138**	**95,943**	**99,789**

(a) There has been some reclassification of expenditure that was previously reported under the Aboriginal advancement nec sub-function (social security and welfare) to other primary functions.

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 Aboriginal and Torres Strait Islander people.

Social security and welfare function expenses are estimated to total around $87.6 billion in 2005-06 and grow significantly over the forward years. The sub-functions contributing most to the growth in the forward years are the assistance to the aged, and assistance to people with disabilities. The main driver in 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. The growth also reflects demographic and social factors such as the ageing of the population and expected developments in the economy and the labour market.

There has been an increase in the assistance to families with children sub-function in 2005-06 and in the forward years due to the increased rate of Family Tax Benefit Part B announced during the election campaign.

Part of the increase in the assistance to the unemployed, assistance to people with disabilities and assistance to families with children sub-functions is a result of the Government's *Welfare to Work* package and changes to Family Tax Benefit arrangements.

Housing and community amenities

Table 10: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Housing	1,457	1,467	1,580	1,618	1,636
Urban and regional development	155	215	148	123	132
Environment protection	274	286	274	251	126
Total housing and community amenities	**1,887**	**1,968**	**2,003**	**1,992**	**1,894**

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.

The moderate growth in the housing sub-function in 2006-07 and 2007-08 is primarily due to the increased expenditure relating to Defence housing requirements, in support of the personnel to be assigned to the Headquarters Joint Operation Command to be located in Bungendore NSW.

The increase in the urban and regional development sub-function in 2005-06 primarily reflects an expansion of the Sustainable Regions Programme. The decrease from 2005-06 to 2007-08 reflects the finalisation of the pilot Sustainable Regions programme and lower expenses under the Regional Partnerships programme.

Expenses under the environment protection sub-function decrease between 2007-08 and 2008-09 due to the termination of funding for the Natural Heritage Trust in 2007-08. The remaining decrease over the two years 2007-08 and 2008-09 reflects the termination in 2007-08 of some measures announced as part of the Climate Change Strategy. These measures are expected to be reviewed and considered in the 2008-09 Budget.

Recreation and culture

Table 11: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Broadcasting	1,191	1,240	1,225	1,238	1,241
Arts and cultural heritage	825	888	876	888	874
Sport and recreation	217	308	242	225	201
National estate and parks	240	234	232	211	156
Total recreation and culture(a)	**2,473**	**2,670**	**2,575**	**2,563**	**2,472**

(a) There has been some reclassification of expenditure that was previously reported under the Aboriginal advancement nec sub-function (Social Security and Welfare) to other primary functions.

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 the 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 fluctuate over the period from 2004-05 to 2008-09. Expenses under the national estate and parks sub-function decrease between 2007-08 and 2008-09 due to the cessation of funding for the Natural Heritage Trust in 2007-08. The growth in the arts and cultural heritage sub-function in 2005-06 reflects in part, increased funding associated with the election commitment A World Class Australian Film Industry.

Higher expenses in the sport and recreational sub-function in 2005-06 primarily reflect a direct payment to the Victorian Government to assist with costs associated with staging the Melbourne 2006 Commonwealth Games. It also reflects additional funding under the programme Building a Healthy, Active Australia — Active After-school Communities. This programme concludes in 2007-08, contributing to the declining trend over the forward years for this sub-function. This trend is partially offset by the additional funding provided for elite sport initiatives in the 2005-06 Budget.

Fuel and energy

Table 12: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Fuel and energy	3,871	4,212	4,198	4,340	4,848
Total fuel and energy	**3,871**	**4,212**	**4,198**	**4,340**	**4,848**

Nature of expenses and major trends

This function includes expenses for the Energy Grants Credits Scheme, Cleaner Fuels Grants Scheme and the Fuels Sales Grants Scheme, which are administered by the Australian Taxation Office. The Business Credits Scheme will replace the Energy Grants Credits Scheme on 1 July 2006.

This function also includes expenses of the Department of the Environment and Heritage for programmes funded under *A New Tax System – Measures for a Better Environment* package, the *Climate Change Strategy* measures and the *Securing Australia's Energy Future* measures. Also included within this function are expenses for programmes relating to the production of alternative fuels including ethanol and biodiesel, which are administered by the Department of Industry, Tourism and Resources and the Australian Taxation Office respectively.

Expenses within this function increase in 2005-06 due to the introduction of the Government's initiative Securing Australia's Energy Future, and an expected increase in outlays in the Energy Grants Credits Scheme as a result of expected improvement in mining production and increases in rail and road transport activity. Following the replacement of the Energy Grants Credits Scheme with the Business Credits Scheme on 1 July 2006, the function is expected to have significant growth from 2006-07 to 2008-09. However growth in 2006-07 will be offset by the cessation of the Fuel Sales Grant Scheme.

Agriculture, forestry and fishing

Table 13: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Wool industry	54	58	59	60	60
Grains industry	125	126	122	121	100
Dairy industry	326	316	307	296	288
Cattle, sheep and pig industry	121	124	123	124	124
Fishing, horticulture and other agriculture	229	202	195	196	190
General assistance not allocated to specific industries	370	378	359	340	324
Rural assistance	457	279	136	59	26
Natural resources development	404	861	1,096	1,041	343
General administration	177	175	172	170	167
Total agriculture, forestry and fishing	**2,263**	**2,520**	**2,571**	**2,408**	**1,622**

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 within this function are expected to increase in 2005-06 and 2006-07 driven by substantial increases in expenditure in the natural resources development sub-function largely due to the expenditure of the Australian Water Fund in 2005-06. The Australian Water Fund will provide $2 billion over six years with significant funding in 2005-06 until 2007-08. The Australian Water Fund will support investment in water infrastructure, improved water management and better practices in the stewardship of Australia's water resources.

The 36 per cent decrease in expenses over the four year period from 2005-06 to 2008-09 reflects the expected cessation of drought related measures within the rural assistance sub-function, due to an assumed return to normal seasonal conditions in Australia. The decrease is also attributable to the termination of funding for the Natural Heritage Trust and the National Action Plan on Salinity and Water Quality under the natural resources development sub-function.

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

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Mining, manufacturing and construction	1,754	1,916	1,820	1,802	1,833
Total mining, manufacturing and construction	**1,754**	**1,916**	**1,820**	**1,802**	**1,833**

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 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, and programmes providing research and development assistance grants and a programme of strategic investment incentives.

The introduction of a new textile clothing and footwear Strategic Investment Programme in 2006-07 will provide a more strategically targeted level of assistance than the current textile clothing and footwear programme over the forward estimates.

The slight decline in expenses from 2006-07 to 2007-08 reflects a lower number of projects being funded under the strategic investment coordination process. Increased expenditure in 2008-09 includes higher grant payments under the Commercial Ready Programme.

Transport and communication

Table 15: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Communication	525	486	421	360	323
Rail transport	15	118	45	31	45
Air transport	156	142	125	125	125
Road transport	1,682	1,670	2,015	2,163	2,021
Sea transport	213	222	234	233	233
Other transport and communication	131	168	132	130	132
Total transport and communication	**2,723**	**2,806**	**2,972**	**3,042**	**2,879**

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 in some sub-functions fluctuate from 2004-05 to 2008-09 reflecting the irregular expenditure patterns associated with the commencement and/or completion of major programmes and one-off projects. The function includes expenses associated with the Government's AusLink national land transport network, involving expenditure on both road and rail.

The decline in the communication sub-function over the period to 2008-09 reflects the conclusion of programmes associated with several Australian Government telecommunication and information technology initiatives, including the Telstra Social Bonus 2, the response to the Telecommunications Service (Besley) Inquiry and the Building on IT strengths Programme.

The increase in the 2005-06 rail transport sub-function reflects rail funding under AusLink and the payment made by the Government to the Australia Rail Track Corporation for new rail infrastructure projects on the interstate rail system.

The high level of expenses in the air transport sub-function in 2004-05 and 2005-06 is primarily due to a one-off funding boost to regional airport security.

The overall increase in the road transport sub-function from 2004-05 to 2008-09 is primarily a result of expenses associated with AusLink. Since the last budget, the Government has increased funding for land transport by approximately $1.2 billion for the five years to 2008-09.

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

	2004-05	**2005-06**	2006-07	2007-08	2008-09
	$m	**$m**	$m	$m	$m
AusLink(a)	1,265	**1,225**	1,562	1,732	1,635
Roads to Recovery	259	**341**	343	330	330
Road Safety Black Spot Programme	45	**45**	45	45	-
Other	113	**59**	65	56	56
Total(b)	**1,682**	**1,670**	**2,015**	**2,163**	**2,021**

(a) Largely Specific Purpose Payments to the states but with a small additional component for land transport research.
(b) See Outcome 1 of the Transport and Regional Services Portfolio Budget Statements 2005-06.

Other economic affairs

Table 16: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Tourism and area promotion	216	204	190	184	129
Vocational and industry training	617	691	744	789	823
Labour market assistance to job seekers and industry	1,940	1,828	1,972	2,062	1,985
Industrial relations	381	271	243	286	259
Immigration	808	899	916	935	969
Total labour and employment affairs	*3,746*	*3,689*	*3,876*	*4,072*	*4,037*
Other economic affairs nec	820	889	857	844	847
Total other economic affairs	**4,782**	**4,782**	**4,923**	**5,100**	**5,013**

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.

Estimates for the labour market assistance to job seekers and industry sub-function reflect an overall increase in resourcing to the Job Network, Work for the Dole and other work assistance programs. The Government's *Welfare to Work* reform package increases the expenditure on labour market assistance to job seekers although this increase is partially offset by improved efficiencies in Job Network arrangements to be implemented from 1 July 2005.

Continuing growth in the vocational and industry training sub-function is due to an expected increase in apprenticeships/traineeships commencements.

The decline between 2007-08 and 2008-09 in the tourism and area promotion sub-function reflects the conclusion of additional funding arrangements announced in the context of the 2003 White Paper on Tourism.

Other purposes

Table 17: Summary of expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Interest on Australian Government's behalf	3,896	3,614	3,532	3,525	3,356
Interest on behalf of states and territories	11	1	0	0	0
Interest received on Australian Government stock	0	0	0	0	0
Public debt interest	*3,907*	*3,614*	*3,532*	*3,525*	*3,356*
Nominal superannuation interest	4,882	5,654	5,478	5,766	5,894
General revenue assistance - states and territories	794	1,146	258	262	97
General capital assistance - states and territories	0	0	0	0	0
Debt assistance	33	220	0	0	0
Local government assistance	1,556	1,628	1,690	1,739	1,804
Revenue assistance to the States and Territories	160	165	169	173	178
Assistance to other governments	493	531	479	475	485
General purpose inter-government transactions	*3,034*	*3,690*	*2,596*	*2,650*	*2,563*
Natural disaster relief	84	104	104	94	94
Contingency reserve(a)	36	187	2,604	4,914	10,095
Total other purposes	**11,943**	**13,250**	**14,314**	**16,948**	**22,002**

(a) Asset sale related expenses are 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.

The increase between 2004-05 and 2005-06 in general revenue assistance to the states and territories reflects compensation for GST revenue forgone to the states and territories in allowing some taxpayers who are voluntarily registered for GST to pay and lodge annually. The decline in this sub-function from 2005-06 reflects the fact that the current National Competition Policy (NCP) agreements only provide for competition payments to 30 June 2006. A Council of Australian Governments (COAG) review of the terms and operation of the NCP arrangements, including an assessment of the future of NCP payments, is scheduled to be completed in 2005. This decline is offset by Budget Balancing Assistance as a result of the Reform of state taxes – payment of Budget Balancing Assistance measure. The Budget Balancing Assistance will facilitate the elimination of a range of inefficient state taxes consistent with the *Intergovernmental Agreement on the Reform of Commonwealth –State Financial Relations*.

The drop-off in the debt assistance sub-function between 2005-06 and 2006-07 reflects the cessation of the agreed debt redemption arrangements between the Australian Government and the states in 2005-06.

The increase between 2004-05 and 2005-06 in the nominal superannuation interest expense for superannuation reflects the increase in the total unfunded liability for the civilian and military schemes, with the balance represented by the increase in the nominal interest rates used by the actuary in calculating military superannuation liabilities.

The increased expenses in the contingency reserve from 2005-06 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 2005-06, forecast net capital investment has increased by $605 million since the 2004-05 MYEFO. This increase is due to the combined effect of new policy decisions of $251 million and parameter and other variations of $354 million.

Net capital investment estimates for the period from 2004-05 to 2008-09 are provided in Table 18.

Table 18: Estimates of total net capital investment

	2004-05		2005-06	2006-07	2007-08	2008-09
	MYEFO(a)	Revised	Estimate	Projections		
Total net capital investment ($m)	**705**	**652**	**1,020**	**617**	**1**	**-264**
Real growth on previous year(%)(b)	6.3	13.4	49.8	-39.9	-99.8	-
Per cent of GDP	0.1	0.1	0.1	0.1	0.0	0.0

(a) As published in the *Mid-Year Economic and Fiscal Outlook 2004-05*.
(b) Real growth is calculated using the non-farm gross domestic product (GDP) deflator.

Net capital investment of $652 million is expected in 2004-05, largely reflecting — various refurbishment/construction projects in the Department of Finance and Administration's property portfolio (such as the construction of the Immigration Reception and Processing Centre on Christmas Island), as well as activities associated with the construction of a nuclear reactor by the Australian Nuclear Science and Technology Organisation; security enhancements of various overseas diplomatic missions, overseen by the Department of Foreign Affairs and Trade (this is partially offset by the re-phasing of land purchases for chanceries in Bangkok, Jakarta and Kuala-Lumpur from 2004-05 into 2005-06); purchase of equipment by the Australian Federal Police for activities in Papua New Guinea, as well as the establishment of a National Protection Operations Centre for Australian diplomats; purchase of biological and chemical agent screening equipment, cargo management information technology infrastructure and new container x-ray machines by the Australian Customs Service; and investment in computer equipment and software by Centrelink. These investments have been partially offset by property sales by the Department of Defence and the Defence Housing Authority.

Reconciliation of net capital investment since the 2004-05 Budget

Table 19 provides a reconciliation of the 2004-05 Budget, 2004-05 MYEFO and 2005-06 Budget net capital investment estimates, showing the effect of policy decisions and economic parameter and other variations since the estimates were published in the 2004-05 Budget.

Table 19: Reconciliation of net capital investment

	Estimates		Projections	
	2004-05	2005-06	2006-07	2007-08
	$m	$m	$m	$m
2004-05 Budget net capital investment	**148**	**45**	**-125**	**-429**
Changes between 2004-05 Budget and MYEFO				
Effect of policy decisions	227	116	104	172
Effect of parameter and other variations	330	254	244	133
Total variations	**557**	**370**	**348**	**304**
2004-05 MYEFO net capital investment	**705**	**415**	**223**	**-125**
Changes between MYEFO and 2005-06 Budget				
Effect of policy decisions	12	251	166	83
Effect of parameter and other variations	-66	354	228	44
Total variations	**-54**	**605**	**394**	**127**
2005-06 Budget net capital investment	**652**	**1,020**	**617**	**1**

Discussion of changes between the 2004-05 MYEFO and the 2005-06 Budget, shown in the table above, can be found in Statement 2 (in the section titled Variations in net capital investment estimates). Further information on capital measures since MYEFO can be found in Budget Paper No. 2, *Budget Measures 2005-06*.

Net capital investment estimates by function

Table 20 provides estimates for Australian Government general government net capital investment by function for the period 2004-05 to 2008-09.

Table 20: Estimates of net capital investment by function

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
General public services	245	624	281	147	-67
Defence	-85	-57	47	-103	-85
Public order and safety	118	55	26	1	6
Education	5	0	1	3	-1
Health	157	21	2	-5	-4
Social security and welfare	59	84	41	-8	-29
Housing and community amenities	95	139	117	-7	-56
Recreation and culture	-50	62	35	-10	-15
Fuel and energy	0	-1	0	0	0
Agriculture, forestry and fishing	0	3	-4	4	4
Mining, manufacturing and construction	5	9	11	8	2
Transport and communications	28	56	-2	-7	-11
Other economic affairs	71	18	32	-5	-5
Other purposes	3	5	29	-17	-3
Total net capital investment	652	1020	617	1	-264

Net capital investment is expected to rise between 2004-05 and 2005-06. This primarily reflects: the construction of the Christmas Island Immigration Reception and Processing Centre, the construction and fit-out of an extension to the Australian Security Intelligence Organisation's Central Office building, and various other construction projects managed by the Department of Finance and Administration; investment by the Australian Nuclear Science and Technology Organisation in a new nuclear reactor; the acquisition of land and refurbishment/security upgrades of various overseas missions by the Department of Foreign Affairs and Trade; and investment in information technology by several departments (including rebuilding the superannuation business system for the Australian Taxation Office and the implementation of the Department of Veterans' Affairs' information technology application development framework). This is partly offset by receipts from property sales by the Department of Defence and the Defence Housing Authority.

After 2005-06, net capital investment is expected to steadily decrease. This results from the conclusion of various construction projects, as well as the progressive conclusion of the Department of Foreign Affairs and Trade's overseas mission upgrades and various information technology-based projects.

Factors contributing to net capital investment, by function, include:

- **General Public Services** - the investment by the Department of Finance and Administration in its property portfolio, including construction of the Adelaide Law Courts building, construction and fit-out of an extension to the Australian Security Intelligence Organisation's Central Office building, and refurbishment of the Royal Australian Mint buildings and ANZAC Park East and West, investment by the Australian Nuclear Science and Technology Organisation in a new nuclear reactor at Lucas Heights, investment by the Commonwealth Scientific and Industrial Research Organisation (CSIRO) in new facilities under the CSIRO Infrastructure Plan, security enhancements, refurbishment and relocation of various overseas missions by the Department of Foreign Affairs and Trade, purchase of equipment by the Australian Federal Police for activities in Papua New Guinea and the Solomon Islands, and the provision of infrastructure in the Indian Ocean Territories by the Department of Transport and Regional Services;

- **Public Order and Safety —** the investment by the Australian Customs Service in additional cargo screening and x-ray equipment, cargo management information technology infrastructure, as well as equipment for the development of biometrics for border control;

- **Health —** the development of information technology systems associated with implementing the pharmaceutical provisions of the Australia-US Free Trade Agreement, developing a database register for a bowel cancer screening programme by the Department of Health and Ageing, and for investment in information technology infrastructure by the Health Insurance Commission for a range of measures, including the creation of eight new Medicare offices;

- **Social Security and Welfare** — the investment in information technology infrastructure for Centrelink;
- **Housing and Community Amenities —** adjustments to the Defence Housing Authority's property portfolio, such as revisions to the estimated timing of certain property sales due to changes in the property market outlook;
- **Recreation and Culture —** the continuation of the facilities upgrade for the Australian Institute of Sport and ongoing capital works at the National Gallery of Australia, offset by the divestment of the Australian Broadcasting Corporation's Gore Hill property in 2004-05 and the sale of radio broadcasting licences in 2004-05. There is also a capital injection in 2005-06 arising from the establishment of the Australian Communications and Media Authority, which follows a return of capital from the amalgamated agencies in 2004-05;
- **Transport and Communications —** the development of information technology systems including the replacement of the Australian Transport Safety Bureau's aviation database and systems for the administration of AusLink; and
- **Other Economic Affairs —** the ongoing replacement and upgrade of various meteorological radars in the Bureau of Meteorology's radar network, as well as the replacement of various meteorological field offices and the purchase of ocean tidal gauges (as part of the Tsunami Early Warning measure), and the upgrade and redevelopment of immigration detention facilities by the Department of Immigration and Multicultural and Indigenous Affairs.

APPENDIX A: EXPENSE BY FUNCTION AND SUB-FUNCTION

Table A1: Estimates of expenses by function and sub-function

	Actuals	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m	$m
General public services						
Legislative and executive affairs	732	850	788	826	941	787
Financial and fiscal affairs	3,522	3,730	3,685	3,864	3,763	3,798
Foreign affairs and economic aid	2,162	2,936	3,063	2,885	3,041	3,138
General research	1,910	2,206	2,324	2,455	2,512	2,509
General services	453	539	576	629	648	657
Government superannuation benefits	2,069	2,487	2,363	2,409	2,434	2,479
Total general public services(a)	**10,848**	**12,748**	**12,799**	**13,067**	**13,339**	**13,368**
Defence	**12,937**	**14,190**	**15,600**	**15,851**	**16,791**	**17,238**
Public order and safety						
Courts and legal services	549	663	716	772	824	832
Other public order and safety	1,837	1,828	2,005	2,020	2,036	2,061
Total public order and safety	**2,386**	**2,490**	**2,721**	**2,792**	**2,860**	**2,892**
Education						
Higher education	4,549	4,735	5,164	5,353	5,528	5,660
Vocational and other education	1,332	1,425	1,571	1,590	1,612	1,635
Non-government schools	4,452	5,091	5,508	5,916	6,338	6,670
Government schools	2,284	2,595	2,851	3,023	3,181	3,234
Schools	*6,735*	*7,686*	*8,359*	*8,939*	*9,519*	*9,904*
Student assistance	650	569	530	547	569	598
General administration	0	1	1	1	1	1
School education - specific funding	130	118	105	111	107	107
Total education	**13,398**	**14,533**	**15,729**	**16,541**	**17,336**	**17,905**
Health						
Medical services and benefits	12,909	14,672	15,688	16,053	16,530	17,067
Hospital services	1,599	1,663	1,808	1,951	2,108	2,272
Health care agreements	7,512	8,008	8,407	8,852	9,310	9,478
Hospital services and health care agreements	*9,110*	*9,671*	*10,214*	*10,803*	*11,418*	*11,750*
Pharmaceutical services and benefits	6,752	7,214	7,536	8,025	8,735	9,615
Aboriginal and Torres Strait Islander health	255	312	374	363	381	408
Health services	963	1,218	1,211	1,207	1,195	1,170
Other health services	1,149	1,566	1,621	1,687	1,752	1,843
Other health services	*2,111*	*2,784*	*2,832*	*2,895*	*2,947*	*3,013*
General administration	506	633	655	654	669	687
Health assistance to the aged	139	254	244	249	257	272
Total health(a)	**31,783**	**35,541**	**37,544**	**39,041**	**40,937**	**42,812**
Social security and welfare						
Assistance to the aged	27,164	28,220	29,876	31,656	33,483	35,310
Assistance to veterans and dependents	5,737	6,017	6,136	6,185	6,220	6,216
Assistance to people with disabilities	10,694	11,658	12,308	12,829	13,454	14,207
Assistance to families with children	24,993	25,458	26,691	27,995	28,584	29,307

Table A1: Estimates of expenses by function and sub-function (continued)

	Actuals	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m	$m
Social security and welfare (continued)						
Assistance to the unemployed	5,443	5,181	5,041	5,676	6,164	6,509
Assistance to the sick	86	87	88	87	86	77
Assistance to the unemployed and the sick	*5,529*	*5,269*	*5,129*	*5,763*	*6,250*	*6,586*
Common youth allowance	2,248	2,219	2,347	2,487	2,545	2,618
Other welfare programmes	637	1,273	1,355	1,422	1,483	1,535
Aboriginal advancement nec(a)	1,429	1,367	1,419	1,452	1,478	1,510
General administration	2,398	2,333	2,302	2,349	2,447	2,499
Total social security and welfare	**80,830**	**83,814**	**87,564**	**92,138**	**95,943**	**99,789**
Housing and community amenities						
Housing	1,247	1,457	1,467	1,580	1,618	1,636
Urban and regional development	138	155	215	148	123	132
Environment protection	250	274	286	274	251	126
Total housing and community amenities	**1,634**	**1,887**	**1,968**	**2,003**	**1,992**	**1,894**
Recreation and culture						
Broadcasting	1,097	1,191	1,240	1,225	1,238	1,241
Arts and cultural heritage	679	825	888	876	888	874
Sport and recreation	207	217	308	242	225	201
National estate and parks	185	240	234	232	211	156
Total recreation and culture(a)	**2,168**	**2,473**	**2,670**	**2,575**	**2,563**	**2,472**
Fuel and energy	**3,502**	**3,871**	**4,212**	**4,198**	**4,340**	**4,848**
Agriculture, forestry and fishing						
Wool industry	57	54	58	59	60	60
Grains industry	129	125	126	122	121	100
Dairy industry	114	326	316	307	296	288
Cattle, sheep and pig industry	130	121	124	123	124	124
Fishing, horticulture and other agriculture	168	229	202	195	196	190
General assistance not allocated to specific industries	384	370	378	359	340	324
Rural assistance	452	457	279	136	59	26
Natural resources development	423	404	861	1,096	1,041	343
General administration	181	177	175	172	170	167
Total agriculture, forestry and fishing	**2,038**	**2,263**	**2,520**	**2,571**	**2,408**	**1,622**
Mining, manufacturing & construction	**1,609**	**1,754**	**1,916**	**1,820**	**1,802**	**1,833**
Transport and communication						
Communication	529	525	486	421	360	323
Rail transport	450	15	118	45	31	45

Table A1: Estimates of expenses by function and sub-function (continued)

	Actuals	Estimates		Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m	$m
Transport and communication (continued)						
Air transport	176	156	142	125	125	125
Road transport	1,356	1,682	1,670	2,015	2,163	2,021
Sea transport	204	213	222	234	233	233
Other transport and communication	101	131	168	132	130	132
Total Transport and Communication	**2,816**	**2,723**	**2,806**	**2,972**	**3,042**	**2,879**
Other economic affairs						
Tourism and area promotion	135	216	204	190	184	129
Vocational and industry training	624	617	691	744	789	823
Labour market assistance to job seekers and industry	1,750	1,940	1,828	1,972	2,062	1,985
Industrial relations	277	381	271	243	286	259
Immigration	753	808	899	916	935	969
Total labour and employment affairs	*3,403*	*3,746*	*3,689*	*3,876*	*4,072*	*4,037*
Other economic affairs nec	748	820	889	857	844	847
Total other economic affairs	**4,286**	**4,782**	**4,782**	**4,923**	**5,100**	**5,013**
Other purposes						
Interest on Australian Government's behalf	3,982	3,896	3,614	3,532	3,525	3,356
Interest on behalf of States and Territories	19	11	1	0	0	0
Interest received on Australian Government stock	0	0	0	0	0	0
Public debt interest	*4,001*	*3,907*	*3,614*	*3,532*	*3,525*	*3,356*
Nominal superannuation interest	4,898	4,882	5,654	5,478	5,766	5,894
General revenue assistance - states and territories	647	794	1,146	258	262	97
General capital assistance - states and territories	0	0	0	0	0	0
Debt assistance	37	33	220	0	0	0
Local government assistance	1,511	1,556	1,628	1,690	1,739	1,804
Revenue assistance to the States and Territories	171	160	165	169	173	178
Assistance to other governments	409	493	531	479	475	485
General purpose inter-government transactions	*2,775*	*3,034*	*3,690*	*2,596*	*2,650*	*2,563*
Natural disaster relief	62	84	104	104	94	94
Contingency reserve(b)	35	36	187	2,604	4,914	10,095
Total other purposes	**11,771**	**11,943**	**13,250**	**14,314**	**16,948**	**22,002**
Total expenses	**182,005**	**195,012**	**206,081**	**214,806**	**225,400**	**236,568**

(a) There has been some reclassification of expenditure that was previously reported under the Aboriginal advancement nec sub-function (social security and welfare) to other primary functions.
(b) 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 the budget and 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;
- 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; 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: DEBT MANAGEMENT

This statement discusses debt management, including maintaining the Commonwealth Government Securities (CGS) market and the proposed investment of financial assets in the Future Fund.

As announced in the 2003-04 Budget, the Government has decided to continue to issue Treasury bonds, despite the Australian Government's strong fiscal position, in order to support low cost interest rate risk management throughout the economy. Treasury bond issuance will be tightly targeted to support the Treasury bond futures market — a key interest rate risk management market.

The Government's decision to establish the Future Fund for the purpose of offsetting unfunded Government superannuation liabilities will not affect the issuance strategy for CGS. Issuance in 2004-05 and planned issuance for 2005-06 reflects the Government's continuing policy stance of maintaining around $5 billion per bond line, which is consistent with continued liquidity. The issuance of Treasury Notes to meet within year financing requirements may increase as a result of transfers of assets to the Future Fund in 2005-06.

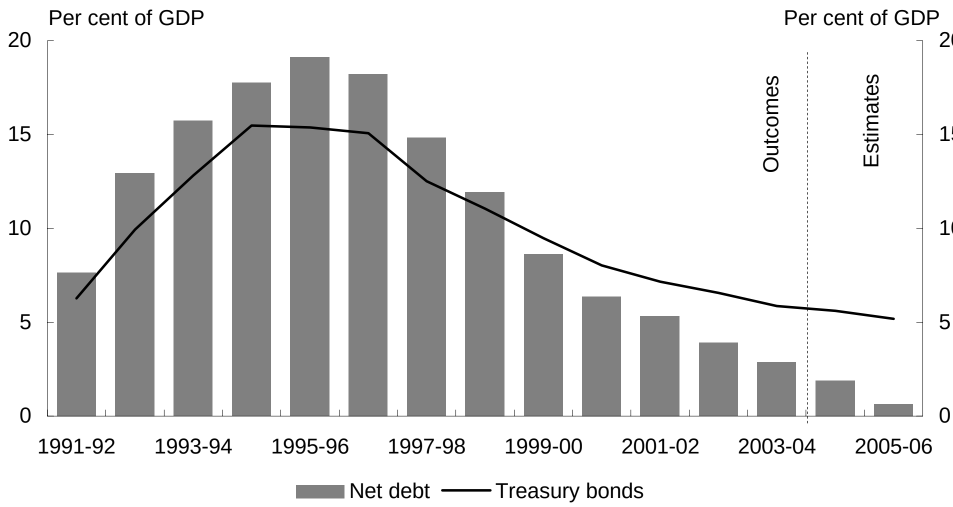
STATEMENT 7: DEBT MANAGEMENT

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 1.9 per cent of GDP or around $16.3 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 per cent of GDP in 2004-05.

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.

In line with the public review of the CGS market in 2002-03 the Government will continue to issue debt, despite a strong fiscal position, in order to maintain a liquid and efficient Treasury bond and Treasury bond futures market. The strategy remains focused on moving towards an issuance pattern that results in around $5 billion in each bond line with a new long and a mid-term bond being issued in alternate years. This will see maturities exceed issuance in some years as the issuance strategy moves towards its long-term steady state.

ESTABLISHMENT OF THE FUTURE FUND

The decision to maintain a CGS market while continuing to achieve a number of budget surpluses has allowed the Australian Government to accumulate significant financial assets, which have been used to assist in meeting within year financing requirements and to reduce the cost of its debt portfolio.

The outstanding stock of CGS is not the only significant liability on the Australian Government's balance sheet. The Australian Government has never fully funded its superannuation liabilities which are now valued at around $91 billion. To offset these superannuation liabilities, the Government will use budget surpluses to build a dedicated financial asset fund — the Future Fund (the Fund). This will reduce calls on the budget in the future, at a time when significant intergenerational pressures are expected to emerge.

The Fund is expected to be established later this year with seed capital sourced from the 2004-05 Budget surplus and from previous surpluses held on deposit at the Reserve Bank, once the Final Budget Outcome for this financial year is known. The Fund will be invested in a broad range of financial assets and will be managed by an independent statutory agency governed by an appropriately qualified board. Contributions to the Fund will be made from future budget surpluses and assets sales with the aim of offsetting the superannuation liability by around 2020. Details of the financial implications of the Fund are in Statement 2.

The decision to establish the Future Fund will not affect the issuance strategy adopted by the Government as a result of the review of the CGS market in 2002-03. Issuance in 2004-05 and planned issuance for 2005-06 reflects the continuing policy stance consistent with maintaining liquidity in the CGS market. The transfer of assets to the Future Fund is likely to necessitate some additional use of Treasury notes to manage the Government's within year financing requirements.

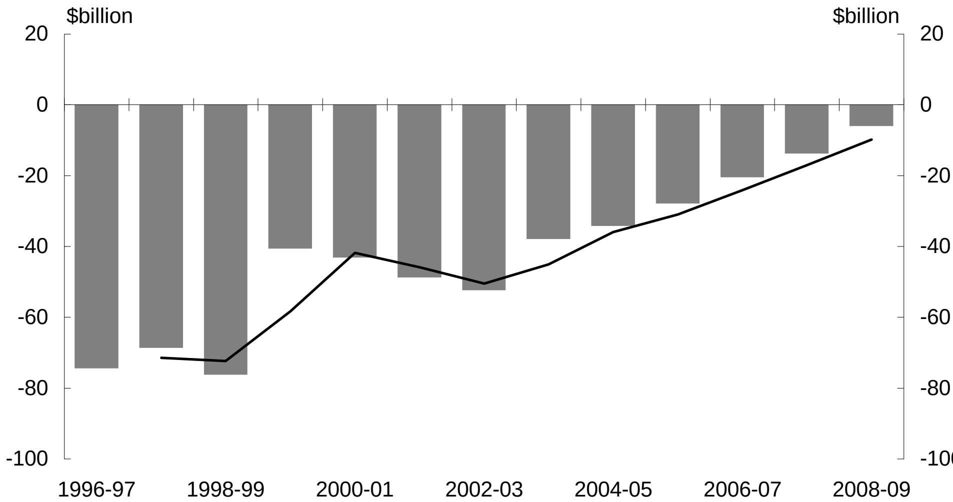
Implications for net debt and net worth

The investment strategy adopted in relation to the Fund will affect the exact impact on the Government's balance sheet. As the Fund and its managing board have not yet been established, standardised assumptions have been made about asset returns for the purposes of this budget. This could mean there will be marginal changes across the forward estimates when the actual initial transfer to the Fund is determined and an asset allocation is set.

Assuming a diversified holding of financial assets, net debt would be expected to rise slightly in the early years. This is because the Government's holdings of cash and fixed-interest securities, including realised budget surpluses, would be converted in part into equities, which will not be offset against gross debt. Beyond the forward estimates period, net debt is expected to fall slowly due to compound growth in the overall asset portfolio, including fixed interest and cash holdings.

Net worth over the forward estimates is likely to improve modestly due to the establishment of the Future Fund because this broader measure includes all assets and liabilities. In addition, transfers of funds between asset classes as the Fund establishes itself will have no impact on net worth. Beyond the forward estimates, net worth is expected to rise steadily due to an expectation of higher average returns on the Fund than current arrangements.

Chart 2: Australian Government general government sector net worth



Source: Australian Bureau of Statistics Cat. No. 5513.0, Australian Government Final Budget Outcomes, Australian Office of Financial Management, and Treasury estimates.

ISSUANCE IN 2004-05 AND 2005-06

The debt issuance programme is directed at maintaining liquid and efficient Treasury bond and Treasury bond futures markets. Accordingly, the volume and timing of Treasury bond issuance takes account of the need to have an appropriate range of Treasury bonds available for inclusion in Treasury bond futures baskets. The programme is moving towards a pattern where new 5-year and 13-year Treasury bonds are launched in alternate years, with total issuance over two years of around $5 billion in each line.

In 2004-05, two new stocks were launched — the February 2017 and August 2010 Treasury bonds. The volumes currently on issue are $3.2 billion for the February 2017 Treasury bond and $2.6 billion for the August 2010 Treasury bond. It is intended to issue a further $600 million of the August 2010 Treasury bond in the period remaining to 30 June 2005.

In the first half of 2005-06, issuance will be focused on the February 2017 Treasury bond and the August 2010 Treasury bond to support the operation of the 3-year and

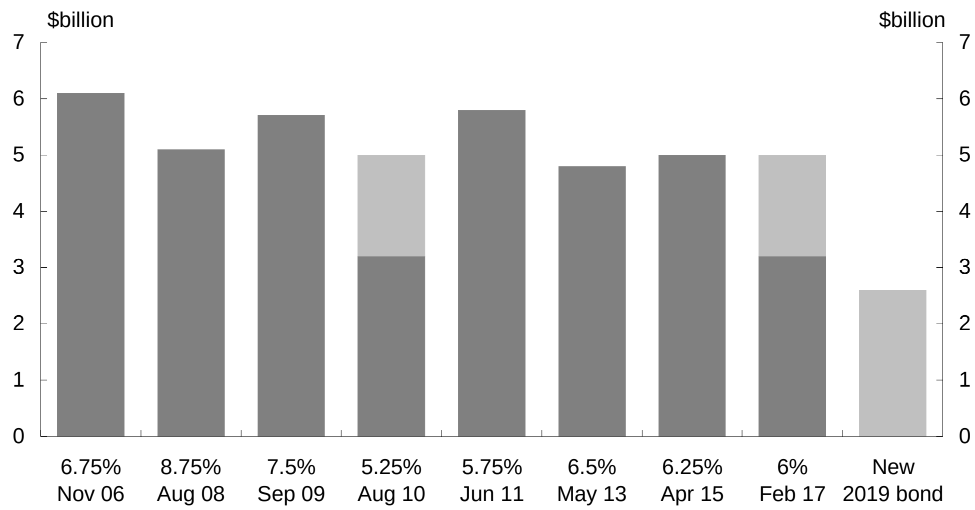
10-year Treasury bond futures contracts. Additional stock will be issued to bring the total volume on issue for each of these bond lines to $5 billion by December 2005.

In early 2006 a new 13-year Treasury bond, a March 2019 bond, will be issued to support the operation of the 10-year Treasury bond futures contract. It is planned to issue $2.6 billion of this new 13-year Treasury bond during 2005-06. The remaining issuance necessary to bring this bond line up to $5 billion will be undertaken in the first half of 2006-07.

Total Treasury bond issuance during 2005-06 will be $6.2 billion, while scheduled maturities during this period, net of Australian Government holdings, are $6.7 billion. As a result, the total stock of Treasury bonds on issue, net of Australian Government holdings, will be around $48 billion at 30 June 2006.

Treasury notes may need to be issued during the financial year to meet within year financing requirements. The magnitude of this issuance will depend on the size and timing of the transfer of assets to the Future Fund.

Chart 3: Benchmark Treasury bonds outstanding expected at 30 June 2006[(a)]



(a) Treasury bonds on issue are net of Australian Government holdings. The October 2007 Treasury bond is excluded from the chart as it is not considered a benchmark bond line.
Note: The dark grey columns represent bonds outstanding at the beginning of the 2005-06 financial year. The light grey columns indicate new issuance in 2005-06.
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 (AAS), including Australian Accounting Standard No. 31 *Financial Reporting by Governments* (AAS 31). 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, the introduction to Statement 9 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 affected 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

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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 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 and volume changes (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 plus Future Fund earnings (GFS surplus/deficit) is the cash counterpart of the fiscal balance, reflecting the Australian Government's cash investment-saving balance. This 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

GFS surplus/deficit

less

Future Fund earnings

equals

Underlying cash balance

The Government is reporting the underlying cash balance net of Future Fund earnings from 2005-06 onwards because the earnings will be reinvested to meet future superannuation payments and are therefore not available for current spending. However, Future Fund earnings are included in the fiscal balance because superannuation expenses relating to future cash payments are recorded in the fiscal balance estimates.

Expected Future Fund earnings are separately identified in the Australian Government cash flow statement in Statement 2 Appendix B and the historic tables in Statement 13.

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.

An underlying cash surplus reflects the extent to which cash is not pre-committed to funding the Australian Government's unfunded superannuation liability and 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 for current period expenditure, 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 and Future Fund earnings 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 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;

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5 Cash flows from investments in financial assets for policy purposes were called net advances under the cash budgeting framework.

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'.

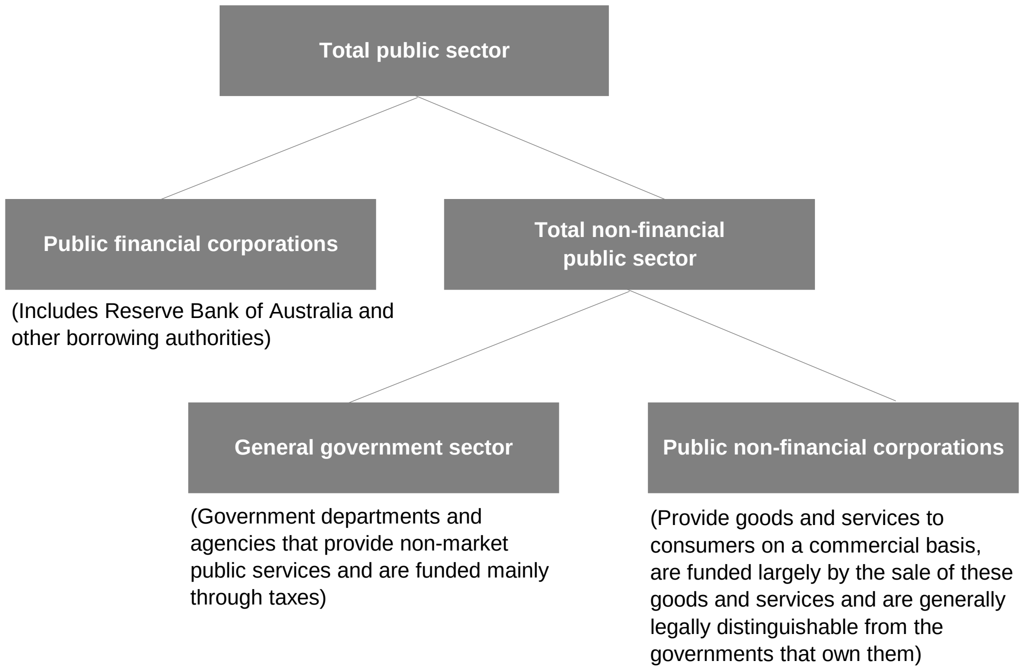
- changes in the valuation of superannuation and employee compensation liabilities due to economic and demographic changes; and
- valuation changes due to movements in foreign exchange rates and interest rates.

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.

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 REPORTING FRAMEWORK, INCLUDING AAS 31

AAS 31 *Financial Reporting by Governments* requires accrual-based general purpose financial reports showing assets, liabilities, revenues, expenses and cash flows, for each government and the entities it controls. Reporting under this framework is intended to provide a consolidated overview of the financial performance and financial position of the Government.

AAS 31 requires, with some stated exceptions, compliance with all other applicable Australian Accounting Standards.

There are three main financial statements required by AAS 31. 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 financial statements, notes to the financial statements are required. These notes include a summary of accounting policies, disaggregated information and other disclosures required by Australian Accounting Standards.

A full set of financial statements for the general government sector, with notes showing disaggregated information, can be found in Statement 10. This includes a note disclosing the anticipated impacts of the Australian Equivalents to International Financial Reporting Standards for the Australian Government from 2005-06.

RECONCILIATION OF GFS AND AAS AGGREGATES

There is a general consistency of treatment of the elements of financial statements between GFS and AAS. 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 AAS definitions of the scope of the public sector agree in almost all cases, with AAS 31 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, AAS is designed 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 AAS 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 AAS 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 AAS 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 AAS and GFS reporting standards

Issue	AAS 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 and 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 AAS. The Australian Accounting Standards Board continues its deliberations in order to harmonise AAS and GFS. A converged financial reporting framework will reduce confusion associated with the publication of two sets of financial statements and improve the readability of government budget and outcome reports.

Table 2 reconciles GFS revenue and expenses with their AAS counterparts.

Table 2: Reconciliation of GFS and AAS revenue and expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
GFS revenue (Statement 9)	**238,966**	**252,511**	**262,942**	**275,675**	**289,846**
less GST revenue for states and territories	36,300	38,000	40,060	42,270	44,520
GFS revenue (Statement 2)	**202,666**	**214,511**	**222,882**	**233,405**	**245,326**
plus asset revenue recognised for the first time	623	124	92	58	58
plus foreign exchange gains	0	0	0	0	0
plus other economic revaluations	134	416	303	257	148
plus proceeds from the sale of assets	823	491	11,655	11,730	11,668
plus swap interest revenue	2,165	2,327	2,250	1,869	1,387
AAS revenue (Statement 10)	**206,411**	**217,869**	**237,182**	**247,319**	**258,587**
GFS expenses (Statement 9)	**230,667**	**243,521**	**254,116**	**266,825**	**280,153**
less GST grants to states and territories	35,550	37,340	39,200	41,320	43,480
less GST mutually agreed writedowns	105	100	110	105	105
GFS expenses (Statement 2)	**195,012**	**206,081**	**214,806**	**225,400**	**236,568**
plus actuarial revaluations	937	0	0	0	0
plus net writedown of assets/bad and doubtful debts	3,026	1,584	1,697	1,723	1,557
plus foreign exchange losses	384	0	0	0	0
plus other economic adjustments	44	0	0	0	0
plus value of assets sold	770	460	2,026	2,121	2,031
plus swap interest expense	1,985	2,225	2,154	1,792	1,317
plus defence weapons platforms depreciation	2,517	2,132	2,166	2,234	2,304
less defence weapons platforms investment	3,064	3,408	3,775	3,988	4,112
plus AusAid IDA/ADF expenses	506	0	0	265	237
plus ETM adjustment for expenses	1,741	0	0	0	0
AAS expenses (Statement 10)	**203,858**	**209,074**	**219,074**	**229,549**	**239,902**

Table 3 reconciles the accounting operating result to the GFS net operating balance and the fiscal balance (GFS net lending).

The AAS net operating result is equal to AAS revenues less expenses. Similarly, GFS revenues less expenses equal the GFS net operating balance. Consequently, the reconciliation between the AAS 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 AAS, there is no equivalent measure to the fiscal balance. That is, the AAS statement of financial performance stops at the operating result and includes no information on net capital investment.

Table 3: Reconciliation of AAS net operating result and fiscal balance

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
AAS operating result before extraordinary items (Statement 10)	**2,554**	**8,794**	**18,108**	**17,770**	**18,685**
Net differences from revenue and expense definitions	5,746	196	-9,282	-8,921	-8,992
GFS net operating balance (Statement 9)	**8,300**	**8,990**	**8,826**	**8,850**	**9,693**
less purchase of property, plant and equipment and intangibles	5,550	6,324	6,145	6,411	6,212
less assets acquired under finance leases	7	4	23	5	4
less other non-financial assets	99	191	179	-110	-89
less increase in inventories	374	340	473	273	270
plus defence weapons platforms investment	3,064	3,408	3,775	3,988	4,112
plus proceeds from sales of property, plant and equipment and intangibles	422	291	175	250	188
plus depreciation and amortisation	4,409	4,272	4,418	4,575	4,665
less weapons depreciation	2,517	2,132	2,166	2,234	2,304
Fiscal balance (GFS net lending) (Statement 9)(a)	**7,648**	**7,970**	**8,208**	**8,848**	**9,957**
Impact of GST	-645	-560	-750	-845	-935
Fiscal balance (GFS net lending) (Statement 2)(a)	**7,003**	**7,410**	**7,458**	**8,003**	**9,022**

(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 *Accrual Uniform Presentation Framework*, except for the departures (other than in relation to the treatment of goods and services tax (GST)) detailed in Appendix A to Statement 2.

In accordance with *Accrual 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 *Accrual Uniform Presentation Framework*, except for the departures (other than in relation to the treatment of goods and services tax (GST)) detailed in Appendix 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. The clear policy intent of the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations*, is that GST is collected by the Australian Taxation Office, as an agent for the states and territories (the states), and appropriated to the states. 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 difference 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 GFS cash surplus/deficit is not affected and provides identical results under both treatments of GST receipts.

The general government sector fiscal balance and net worth include an allowance, through the contingency reserve, for the anticipated impact of Australian Equivalents to International Financial Reporting Standards. The Australian Government general government sector fiscal balance increases by $57 million in 2005-06 due to lower expenses with minor impacts in the forward years. Australian Government general

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.

government sector net worth reduces by around $1.3 billion in 2005-06 and the forward years.

Transactions between the Australian Government general government and public non-financial corporations are included in the relevant tables, but removed from the total non-financial public sector tables as they are transactions internal to that sector.

Public access communication assets, computer software and other intangibles are recorded at historic costs, as market value information, or suitable proxies for market value, are not readily observable. This affects the public non-financial corporations sector balance sheet, but does not affect the general government sector balance sheet.

Statement 8 provides reconciliations between key GFS aggregates and their Australian Accounting Standards counterparts.

In accordance with *Accrual Uniform Presentation Framework* requirements, this statement also contains an update of the Australian Government's Loan Council Allocation.

GOVERNMENT FINANCE STATISTICS STATEMENTS

Table 1: Australian Government general government sector operating statement

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
GFS revenue					
Taxation revenue	226,501	239,267	249,059	261,068	274,640
Current grants and subsidies	0	0	0	0	0
Sales of goods and services	4,828	4,965	5,194	5,330	5,363
Interest income	1,562	2,000	2,853	3,997	5,025
Dividend income	3,146	3,312	2,952	2,357	1,852
Other	2,929	2,967	2,884	2,924	2,966
Total GFS revenue	**238,966**	**252,511**	**262,942**	**275,675**	**289,846**
GFS expenses					
Gross operating expenses					
Depreciation	1,892	2,140	2,252	2,341	2,361
Superannuation	2,487	2,363	2,409	2,434	2,479
Salaries and wages	11,922	12,617	12,828	13,164	13,668
Payment for supply of goods and services	45,246	48,395	50,538	52,858	54,020
Other operating expenses	2,814	2,584	2,618	2,770	2,917
Total gross operating expenses	*64,362*	*68,100*	*70,645*	*73,567*	*75,444*
Nominal superannuation interest expense	4,882	5,713	5,594	5,821	5,947
Other interest expenses	4,131	3,851	3,774	3,761	3,574
Other property expenses	0	0	0	0	0
Current transfers					
Grant expenses	72,753	77,899	79,942	83,613	86,372
Subsidy expenses	6,470	6,560	6,697	6,936	7,466
Personal benefit payments in cash	74,478	77,545	83,258	88,742	97,033
Other current transfers	0	0	0	0	0
Total current transfers	*153,701*	*162,004*	*169,897*	*179,292*	*190,870*
Capital transfers	3,591	3,854	4,207	4,384	4,318
Total GFS expenses	**230,667**	**243,521**	**254,116**	**266,825**	**280,153**
Net operating balance(a)	**8,300**	**8,990**	**8,826**	**8,850**	**9,693**
Net acquisition of non-financial assets					
Purchases of non-financial assets	2,487	2,920	2,392	2,429	2,104
less Sales of non-financial assets	364	285	174	250	188
less Depreciation	1,892	2,140	2,252	2,341	2,361
plus Change in inventories	374	340	473	273	270
plus Other movements in non-financial assets	47	185	178	-111	-89
Total net acquisition of non-financial assets	**652**	**1,020**	**617**	**1**	**-264**
Net lending/fiscal balance(a)(b)	**7,648**	**7,970**	**8,208**	**8,848**	**9,957**

(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

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
GFS assets					
Financial assets					
Cash and deposits	927	288	459	210	143
Advances paid	19,314	20,536	22,001	23,921	26,059
Investments, loans and placements(a)	31,066	38,096	56,389	77,150	96,186
Other non-equity assets	19,472	20,450	22,517	24,896	27,565
Equity(b)	50,895	51,137	40,166	28,854	17,570
Total financial assets	121,675	130,507	141,532	155,031	167,523
Non-financial assets					
Land	4,863	5,161	5,119	5,027	4,973
Buildings	13,894	14,008	14,263	14,428	14,536
Plant, equipment and infrastructure	8,411	8,578	8,716	8,546	8,256
Inventories	5,299	5,570	5,989	6,228	6,463
Heritage and cultural assets	6,698	6,739	6,766	6,787	6,808
Other non-financial assets	2,085	2,341	2,207	2,006	1,762
Total non-financial assets	*41,250*	*42,397*	*43,060*	*43,022*	*42,798*
Total GFS assets	**162,925**	**172,904**	**184,593**	**198,053**	**210,320**
GFS liabilities					
Deposits held	365	365	365	365	365
Advances received	0	0	0	0	0
Government securities(a)	61,452	59,284	59,106	60,932	60,633
Loans	5,595	5,164	5,190	5,212	4,912
Other borrowing	224	189	158	124	90
Superannuation liability	91,071	95,578	98,801	101,997	105,168
Other employee entitlements and provisions	7,605	7,812	7,918	8,080	8,266
Other non-equity liabilities	28,654	29,937	30,675	31,731	32,893
Total GFS liabilities	**194,966**	**198,327**	**202,213**	**208,440**	**212,327**
Net worth(c)(d)	**-32,040**	**-25,423**	**-17,620**	**-10,387**	**-2,006**
Net financial worth(e)	-73,291	-67,820	-60,680	-53,409	-44,804
Net debt(f)	16,328	6,080	-14,031	-34,649	-56,389

(a) For 2005-06 and the forward years, the netting of assets — investments, loans and placements and liabilities — government securities has been removed so that both lines are now reported on a gross basis.

(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) 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.

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

(e) Net financial worth equals total financial assets minus total liabilities. That is, it excludes non-financial assets.

(f) 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)]

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Cash receipts from operating activities					
Taxes received(b)	221,796	235,149	244,174	256,102	269,378
Receipts from sales of goods and services(c)	4,814	4,971	5,186	5,322	5,355
Grants and subsidies received	0	0	0	0	0
Interest receipts	1,460	1,828	2,649	3,783	4,789
Dividends	3,808	3,632	2,952	2,357	1,852
GST input credits received by general government(c)	0	0	0	0	0
Other receipts	2,849	2,926	2,875	2,851	2,938
Total operating receipts	**234,727**	**248,506**	**257,836**	**270,414**	**284,313**
Cash payments for operating activities					
Payments for goods and services(c)	-45,570	-48,518	-50,850	-53,025	-54,211
Grants and subsidies paid(d)	-80,750	-86,535	-89,485	-93,487	-96,233
Interest paid	-3,856	-4,587	-3,808	-3,534	-3,450
Personal benefit payments	-73,664	-76,487	-82,415	-88,071	-96,604
Salaries, wages and other entitlements	-16,508	-17,102	-17,371	-18,002	-18,693
GST payments by general government to taxation authority(c)	0	0	0	0	0
Other payments for operating activities	-2,988	-3,079	-2,635	-2,730	-2,958
Total operating payments	**-223,336**	**-236,308**	**-246,562**	**-258,849**	**-272,148**
Net cash flows from operating activities	**11,391**	**12,198**	**11,273**	**11,565**	**12,165**
Cash flows from investments in non-financial assets					
Sales of non-financial assets	416	291	175	250	188
Purchases of non-financial assets	-2,579	-3,102	-2,549	-2,313	-2,011
Net cash flows from investments in non-financial assets	**-2,163**	**-2,812**	**-2,374**	**-2,063**	**-1,823**
Net cash flows from investments in financial assets for policy purposes	**-1,317**	**-1,518**	**9,286**	**9,054**	**9,022**
Cash flows from investments in financial assets for liquidity purposes					
Increase in investments	-7,456	-7,217	-18,306	-20,751	-19,023
Net cash flows from investments in financial assets for liquidity purposes	**-7,456**	**-7,217**	**-18,306**	**-20,751**	**-19,023**
Cash flows from financing activities					
Advances received (net)	0	0	0	0	0
Borrowing (net)	188	-1,579	-30	1,928	-481
Deposits received (net)	0	0	0	0	0
Other financing (net)	-1,306	288	322	18	72
Net cash flows from financing activities	**-1,118**	**-1,291**	**291**	**1,946**	**-408**
Net increase/decrease in cash held	**-663**	**-639**	**171**	**-249**	**-67**
Net cash from operating activities and investments in non-financial assets	**9,227**	**9,387**	**8,899**	**9,502**	**10,342**
Finance leases and similar arrangements(e)	-7	-4	-23	-5	-4
Equals surplus(+)/deficit(-)	**9,221**	**9,383**	**8,876**	**9,497**	**10,338**

(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 is $41 million greater in 2004-05 than GST cash receipts measured on a state tax basis (as shown in Statement 10, Note 18).
(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)

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Opening net worth	**-36,165**	**-32,040**	**-25,423**	**-17,620**	**-10,387**
Opening net worth adjustments(a)	**-1,741**	**0**	**0**	**0**	**0**
Adjusted opening net worth	**-37,906**	**-32,040**	**-25,423**	**-17,620**	**-10,387**
Change in net worth from operating transactions	8,300	8,990	8,826	8,850	9,693
Change in net worth from other economic flows					
Revaluation of equity(b)	1,301	261	322	-19	4
Net writedowns of assets (including bad and doubtful debts)	-2,423	-1,737	-1,955	-2,018	-1,646
Assets recognised for the first time	23	94	80	58	58
Liabilities recognised for the first time	0	0	0	0	0
Actuarial revaluations	-937	0	0	0	0
Net foreign exchange gains	-384	0	0	0	0
Net swap interest received	180	102	96	77	70
Market valuation of debt	-195	371	303	257	148
Other economic revaluations(c)	2	-1,463	131	29	53
Total other economic flows	**-2,433**	**-2,373**	**-1,022**	**-1,616**	**-1,313**
Closing net worth	**-32,040**	**-25,423**	**-17,620**	**-10,387**	**-2,006**

(a) Decrease in net worth arising from a change in recognition of family tax benefits and other expenses from a cash to an accrual basis.

(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) Largely reflects revaluation of assets and liabilities and Australian Equivalents to International Financial Reporting Standards adjustments.

Table 5: Australian Government public non-financial corporations operating statement

	Estimates	
	2004-05	2005-06
	$m	$m
GFS revenue		
Current grants and subsidies	353	358
Sales of goods and services	26,221	27,307
Interest income	117	112
Other	1	1
Total GFS revenue	**26,693**	**27,778**
GFS expenses		
Gross operating expenses		
Depreciation	3,561	3,919
Salaries, wages and other entitlements	5,810	5,957
Other operating expenses	11,486	12,394
Total gross operating expenses	*20,857*	*22,270*
Interest expenses	322	466
Other property expenses	1,674	2,095
Current transfers		
Tax expenses	2,071	2,055
Other current transfers	0	0
Total current transfers	*2,071*	*2,055*
Capital transfers	0	0
Total GFS expenses	**24,924**	**26,886**
Net operating balance	**1,769**	**892**
Net acquisition of non-financial assets		
Purchases of non-financial assets	4,412	4,604
less Sales of non-financial assets	159	51
less Depreciation	3,561	3,919
plus Change in inventories	24	43
plus Other movements in non-financial assets	-420	1
Total net acquisition of non-financial assets	**295**	**679**
Net lending/fiscal balance(a)	**1,475**	**213**

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

Table 6: Australian Government public non-financial corporations balance sheet

	Estimates	
	2004-05	2005-06
	$m	$m
GFS assets		
Financial assets		
Cash and deposits	1,913	1,668
Advances paid	0	0
Investments, loans and placements	234	194
Other non-equity assets	5,288	5,403
Equity	304	545
Total financial assets	*7,738*	*7,810*
Non-financial assets		
Land and fixed assets	26,442	26,714
Other non-financial assets(a)	2,171	2,496
Total non-financial assets	*28,613*	*29,210*
Total GFS assets	**36,351**	**37,020**
GFS liabilities		
Deposits held	0	0
Advances received	0	0
Borrowing	12,692	12,645
Unfunded superannuation liability and other employee entitlements	2,018	2,206
Provisions (other than depreciation and bad and doubtful debts)(a)	3,002	3,012
Other non-equity liabilities	1,678	1,768
Total GFS liabilities	**19,390**	**19,631**
Shares and other contributed capital	**67,553**	**67,790**
Net worth(b)	**-50,592**	**-50,401**
Net financial worth(c)	-79,205	-79,611
Net debt(d)	10,546	10,783

(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)]

	Estimates	
	2004-05	2005-06
	$m	$m
Cash receipts from operating activities		
Receipts from sales of goods and services	26,048	27,308
Grants and subsidies received	50	120
GST input credit receipts	61	61
Other receipts	230	204
Total operating receipts	**26,390**	**27,694**
Cash payments for operating activities		
Payment for goods and services	-8,691	-9,363
Interest paid	-155	-299
Salaries, wages and other entitlements	-5,838	-5,879
GST payments to taxation authority	-1,263	-1,265
Other payments for operating activities(b)	-3,230	-3,817
Total operating payments	**-19,178**	**-20,623**
Net cash flows from operating activities	**7,212**	**7,070**
Cash flows from investments in non-financial assets		
Sales of non-financial assets	177	58
Purchases of non-financial assets	-4,416	-4,610
Net cash flows from investments in non-financial assets	**-4,239**	**-4,552**
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	223	-202
Net cash flows from investments in financial assets for liquidity purposes	**223**	**-202**
Cash flows from financing activities		
Advances received (net)	0	0
Borrowing (net)	-129	56
Deposits received (net)	0	0
Distributions paid (net)(c)	-1,685	-2,085
Other financing (net)	-1,358	-532
Net cash flows from financing activities	**-3,172**	**-2,561**
Net increase/decrease in cash held	**25**	**-245**
Net cash from operating activities and investments in non-financial assets	**2,973**	**2,518**
Finance leases and similar arrangements(d)	0	0
Distributions paid(c)	-1,685	-2,085
Equals surplus(+)/deficit(-)	**1,288**	**433**

(a) A positive number denotes a cash inflow; a negative sign denotes a cash outflow.
(b) Other payments for operating activities includes the cash flow to the general government sector from public non-financial corporations distributions paid.
(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

	Estimates	
	2004-05	2005-06
	$m	$m
GFS revenue		
Taxation revenue	224,431	237,212
Current grants and subsidies	0	0
Sales of goods and services	30,513	31,667
Interest income	1,679	2,112
Dividend income	1,143	819
Other	2,930	2,968
Total GFS revenue	**260,695**	**274,778**
GFS expenses		
Gross operating expenses		
Depreciation	5,453	6,059
Superannuation	2,540	2,454
Salaries and wages	17,732	18,574
Payment for supply of goods and services	53,878	57,331
Other operating expenses	3,076	2,854
Total gross operating expenses	*82,679*	*87,272*
Nominal superannuation interest expense	4,882	5,713
Other interest expenses	4,454	4,317
Other property expenses	1,674	2,095
Current transfers		
Grant expenses	72,753	77,899
Subsidy expenses	6,117	6,201
Personal benefit payments in cash	74,478	77,545
Other current transfers	0	0
Total current transfers	*153,348*	*161,646*
Capital transfers	3,591	3,854
Total GFS expenses	**250,627**	**264,896**
Net operating balance(a)	**10,069**	**9,882**
Net acquisition of non-financial assets		
Purchases of non-financial assets	6,899	7,524
less Sales of non-financial assets	523	336
less Depreciation	5,453	6,059
plus Change in inventories	397	384
plus Other movements in non-financial assets	-373	186
Total net acquisition of non-financial assets	**946**	**1,699**
Net lending/fiscal balance(a)(b)	**9,123**	**8,183**

(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

	Estimates	
	2004-05	2005-06
	$m	$m
GFS assets		
Financial assets		
Cash and deposits	2,840	1,956
Advances paid	19,314	20,536
Investments, loans and placements	31,300	38,290
Other non-equity assets	24,745	25,837
Equity	14,663	14,909
Total financial assets	*92,863*	*101,529*
Non-financial assets		
Land and fixed assets	65,607	66,769
Other non-financial assets	4,256	4,837
Total non-financial assets	*69,863*	*71,607*
Total GFS assets	**162,726**	**173,136**
GFS liabilities		
Deposits held	365	365
Advances received	0	0
Government securities	61,452	59,284
Loans	5,595	5,164
Other borrowing	12,916	12,834
Unfunded superannuation liability and other employee entitlements	100,694	105,595
Other provisions	6,868	7,019
Other non-equity liabilities	26,451	27,682
Total GFS liabilities	**214,341**	**217,943**
Shares and other contributed capital	**31,017**	**31,017**
Net worth(a)	**-82,633**	**-75,824**
Net financial worth(b)	-152,496	-147,431
Net debt(c)	26,874	16,863

(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 financial worth equals total financial assets minus total liabilities minus shares and other contributed capital. That is, it excludes non-financial assets.

(c) 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)]

	Estimates	
	2004-05	2005-06
	$m	$m
Cash receipts from operating activities		
Taxes received	218,469	231,838
Receipts from sales of goods and services(b)	30,846	32,262
Grants and subsidies received	0	0
Interest receipts	1,578	1,940
Dividends	1,805	1,139
GST input credit receipts(b)	0	0
Other receipts	2,961	3,019
Total operating receipts	**255,659**	**270,197**
Cash payments for operating activities		
Payments for goods and services(b)	-54,192	-57,812
Grants and subsidies paid	-80,700	-86,414
Interest paid	-4,011	-4,886
Personal benefit payments	-73,664	-76,487
Salaries, wages and other entitlements	-22,345	-22,980
GST payments to taxation authority(b)	0	0
Other payments for operating activities	-2,144	-2,348
Total operating payments	**-237,056**	**-250,929**
Net cash flows from operating activities	**18,603**	**19,269**
Cash flows from investments in non-financial assets		
Sales of non-financial assets	593	349
Purchases of non-financial assets	-6,996	-7,712
Net cash flows from investments in non-financial assets	**-6,402**	**-7,364**
Net cash flows from investments in financial assets for policy purposes	**-1,317**	**-1,518**
Cash flows from investments in financial assets for liquidity purposes		
Increase in investments	-7,233	-7,419
Net cash flows from investments in financial assets for liquidity purposes	**-7,233**	**-7,419**
Cash flows from financing activities		
Advances received (net)	0	0
Borrowing (net)	59	-1,523
Deposits received (net)	0	0
Distributions paid (net)(c)	-1,685	-2,085
Other financing (net)	-2,664	-244
Net cash flows from financing activities	**-4,290**	**-3,852**
Net increase/decrease in cash held	**-638**	**-884**
Net cash from operating activities and investments in non-financial assets	**12,201**	**11,905**
Finance leases and similar arrangements(d)	-7	-4
Distributions paid(c)	-1,685	-2,085
Equals surplus(+)/deficit(-)	**10,509**	**9,815**

(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

	Estimates	
	2004-05	2005-06
	$m	$m
Taxes on income, profits and capital gains		
Income and capital gains levied on individuals	109,220	112,820
Income and capital gains levied on enterprises	47,160	54,460
Income taxes levied on non-residents	0	0
Total taxes on income, profits and capital gains	**156,380**	**167,280**
Taxes on employers' payroll and labour force	3,297	3,580
Taxes on property	14	14
Taxes on the provision of goods and services		
Sales/goods and services tax	37,480	39,230
Excises and levies	22,814	23,284
Taxes on international trade	5,714	5,071
Other	0	0
Total taxes on the provision of goods and services	**66,008**	**67,585**
Taxes on use of goods and performance of activities	803	808
Total GFS taxation revenue	**226,501**	**239,267**

Table 12: Australian Government purchases of non-financial assets by function

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
General public services	831	1,029	680	875	567
Defence	615	1,202	589	654	1,000
Public order and safety	224	190	169	150	166
Education	16	12	12	15	12
Health	103	99	88	83	83
Social security and welfare	219	285	254	215	171
Housing and community amenities	8	36	50	44	41
Recreation and culture	263	4	260	217	212
Fuel and energy	3	4	4	3	4
Agriculture, forestry and fishing	27	32	25	33	33
Mining, manufacturing and construction	30	37	38	35	29
Transport and communications	-65	-206	38	36	36
Other economic affairs	210	184	198	174	182
Other purposes	5	14	-12	-107	-431
General government purchases of non-financial assets	**2,487**	**2,920**	**2,392**	**2,429**	**2,104**

APPENDIX A: AUSTRALIAN 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 2005-06 Loan Council Allocation Budget update is a $8,432 million surplus. This compares with the Australian Government's nominated, and Loan Council endorsed, Loan Council Allocation surplus of $5,972 million.

Table 13: Australian Government's Loan Council Allocation Budget update for 2005-06

	2005-06 Nomination $m	2005-06 Budget Estimate $m
General government sector cash deficit(+)/surplus(-)	-4,459	-9,383
Public non-financial corporations sector cash deficit(+)/surplus(-)	-1,914	-433
Non-financial public sector cash deficit(+)/surplus(-)	-6,374	-9,815
less Net cash flows from investments in financial assets for policy purposes(a)	-1,441	-1,518
plus Memorandum items(b)	-1,039	-135
Loan Council Allocation	**-5,972**	**-8,432**

(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 include the change in net present value (NPV) of operating leases (with NPV greater than $5 million) and over-funding of superannuation.

Statement 10: Australian Accounting Standards Financial Statements

This statement provides financial tables prepared on an accrual basis in accordance with applicable Australian Accounting Standards (AAS), including Australian Accounting Standard No. 31 *Financial Reporting by Governments*, except where departures from the standards are identified in Note 1.

A reconciliation between the Australian Government's general government AAS 31 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

	Note	Estimates		Projections		
		2004-05	2005-06	2006-07	2007-08	2008-09
		$m	$m	$m	$m	$m
Revenues						
Taxation						
Income taxation	4	156,380	167,280	174,460	183,430	193,930
Indirect taxation	5	28,904	28,791	29,252	30,032	30,762
Fringe benefits tax		3,050	3,350	3,380	3,480	3,580
Other taxes		1,636	1,635	1,714	1,681	1,689
Total taxation revenue		**189,970**	**201,055**	**208,806**	**218,623**	**229,961**
Non-taxation						
Sales of goods and services		4,900	5,031	5,254	5,384	5,413
Interest and dividends	6	6,873	7,639	8,055	8,222	8,264
Net foreign exchange gains		0	0	0	0	0
Proceeds from the sale of assets		823	491	11,655	11,730	11,668
Other sources of non-taxation revenue	7	3,845	3,652	3,412	3,359	3,282
Total non-taxation revenue		**16,442**	**16,813**	**28,376**	**28,696**	**28,625**
Total revenue		**206,411**	**217,869**	**237,182**	**247,319**	**258,587**
Expenses						
Goods and services						
Employees	8	22,911	23,277	23,449	24,190	25,010
Suppliers	9	16,848	17,893	17,968	18,321	17,592
Depreciation and amortisation	10	4,409	4,272	4,418	4,575	4,665
Net writedown of assets		3,434	2,129	2,197	2,239	2,340
Net foreign exchange losses		384	0	0	0	0
Value of assets sold		770	460	2,211	2,296	2,188
Other goods and services expenses	11	7,078	7,479	8,046	8,388	8,730
Total goods and services		**55,834**	**55,511**	**58,289**	**60,009**	**60,524**
Subsidies benefits and grants						
Personal benefits		91,137	93,667	100,019	106,534	115,979
Subsidies		11,212	11,395	11,868	12,498	13,374
Grants	12	39,474	42,414	42,970	44,954	45,134
Total subsidies benefits and grants		**141,823**	**147,477**	**154,857**	**163,986**	**174,487**
Borrowing costs						
Interest		6,186	6,070	5,905	5,538	4,881
Other borrowing costs		15	17	22	15	9
Total interest and other borrowing costs		**6,200**	**6,087**	**5,928**	**5,553**	**4,890**
Total expenses		**203,858**	**209,074**	**219,074**	**229,549**	**239,902**
Operating result		**2,554**	**8,794**	**18,108**	**17,770**	**18,685**

Table 2: Statement of financial position for the Australian Government general government sector

	Note	Estimates		Projections		
		2004-05	2005-06	2006-07	2007-08	2008-09
		$m	$m	$m	$m	$m
Assets						
Financial assets						
Cash		927	288	459	210	143
Receivables	13	29,829	31,878	34,982	38,461	42,187
Investments(a)		47,263	54,462	71,121	90,198	107,577
Equity accounted investments		402	402	402	402	402
Accrued revenue		490	506	549	598	663
Other financial assets		18	19	18	18	19
Total financial assets		**78,929**	**87,554**	**107,530**	**129,887**	**150,991**
Non-financial assets	14					
Land and buildings		18,757	19,169	19,382	19,455	19,509
Infrastructure		39,398	40,773	42,470	44,015	45,501
Heritage and cultural assets		6,698	6,739	6,766	6,787	6,808
Intangibles		1,693	1,758	1,711	1,672	1,610
Inventories		5,299	5,570	5,989	6,228	6,463
Other non-financial assets		1,832	1,743	1,627	1,474	1,293
Total non-financial assets		**73,678**	**75,751**	**77,945**	**79,631**	**81,184**
Total assets		**152,607**	**163,305**	**185,475**	**209,518**	**232,174**
Liabilities						
Debt						
Government securities(a)		55,705	56,428	56,016	57,643	57,283
Loans		4,537	4,099	4,117	4,136	3,834
Leases		201	165	135	102	69
Deposits		365	365	365	365	365
Overdrafts		0	0	0	0	0
Other debt		1,076	880	949	976	1,010
Total debt		**61,885**	**61,936**	**61,581**	**63,221**	**62,560**
Provisions and payables						
Employees and superannuation	15	98,676	103,390	106,720	110,076	113,434
Suppliers		2,145	2,198	2,173	2,171	2,172
Personal benefits payable		8,347	9,334	9,903	10,518	10,966
Subsidies payable		912	790	731	683	689
Grants payable	16	9,842	10,035	10,019	10,365	10,891
Other provisions and payables		10,596	10,201	10,704	11,048	11,291
Total provisions and payables		**130,519**	**135,948**	**140,250**	**144,862**	**149,443**
Total liabilities		**192,403**	**197,885**	**201,831**	**208,083**	**212,003**
Net assets	17	**-39,797**	**-34,579**	**-16,357**	**1,435**	**20,171**
Equity						
Accumulated results		-75,157	-69,887	-50,122	-30,701	-10,379
Reserves		35,361	35,308	33,765	32,136	30,550
Capital		0	0	0	0	0
Total equity		**-39,797**	**-34,579**	**-16,357**	**1,435**	**20,171**

(a) For 2004-05 and the forward years, the netting of assets — investments — and liabilities — government securities — has been revised so that both lines are now reported on a gross basis.

Table 3: Statement of cash flows for the Australian Government general government sector

	Note	Estimates		Projections		
		2004-05	2005-06	2006-07	2007-08	2008-09
		$m	$m	$m	$m	$m
Operating activities						
Cash received						
Taxation	18	186,133	197,763	204,915	214,727	225,845
Sales of goods and services		5,087	5,231	5,445	5,581	5,614
Interest		3,537	4,147	4,921	5,753	6,252
Dividends		3,808	3,632	2,952	2,357	1,852
GST input credit receipts		2,908	2,844	2,882	2,976	3,018
Other		2,931	2,971	2,875	2,851	2,938
Total operating cash received		**204,405**	**216,588**	**223,988**	**234,244**	**245,520**
Cash used						
Payments to employees		19,496	19,617	20,006	20,731	21,551
Payments to suppliers		20,255	21,054	21,342	21,581	20,951
Subsidies paid		10,127	10,906	11,325	11,944	12,766
Personal benefits		88,867	92,610	99,176	105,863	115,550
Grant payments		38,352	41,922	42,924	44,582	44,587
Interest and other financing costs		5,995	6,832	5,938	5,657	5,043
GST payments to taxation authority		120	120	122	123	124
Other		6,859	7,942	7,943	8,352	8,661
Total operating cash used		**190,072**	**201,005**	**208,776**	**218,834**	**229,233**
Net cash from operating activities		**14,333**	**15,583**	**15,212**	**15,410**	**16,287**
Investing activities						
Cash received						
Proceeds from asset sales program		0	0	11,280	11,280	11,280
Proceeds from sales of property, plant and equipment and intangibles		422	291	175	250	188
Net loans, advances and HECS		0	0	0	0	0
Other net investing cash received		401	200	200	200	200
Total investing cash received		**823**	**491**	**11,655**	**11,730**	**11,668**
Cash used						
Purchase of property, plant and equipment and intangibles		5,652	6,506	6,327	6,301	6,122
Net loans, advances and HECS		1,135	1,365	1,831	2,062	2,141
Other net investing cash paid		7,854	7,422	18,687	21,126	19,380
Total investing cash used		**14,640**	**15,293**	**26,846**	**29,488**	**27,643**
Net cash from investing activities		**-13,818**	**-14,802**	**-15,191**	**-17,758**	**-15,976**
Financing activities						
Cash received						
Net cash received from currency issues		0	0	0	0	0
Other		0	199	233	209	139
Total financing cash received		**0**	**199**	**233**	**209**	**139**
Cash used						
Net repayments of borrowings		-188	1,579	30	-1,928	481
Other		1,366	40	53	38	37
Total financing cash used		**1,178**	**1,619**	**83**	**-1,890**	**518**
Net cash from financing activities		**-1,178**	**-1,420**	**150**	**2,099**	**-379**
Net increase/decrease in cash held	3	**-663**	**-639**	**171**	**-249**	**-67**

NOTES TO THE AAS FINANCIAL STATEMENTS

Note 1: External reporting standards and accounting policies

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 (AAS), including AAS31 *Financial Reporting by Governments* (AAS31).

AAS requires governments to prepare accrual based general purpose financial reports. This means that assets, liabilities, revenues and expenses are recorded in financial statements when transactions have an economic impact on the government, rather than when the cash flow associated with these transactions occurs. Consistent with AAS, 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.

AAS will change from 2005-06, with the introduction of Australian Equivalents to International Financial Reporting Standards (AEIFRS). The tables in this Statement are presented on the basis of Australian Accounting Standards as at the date of preparation of the Budget. However, the amounts presented in these financial statements have been adjusted to include the material, reliably estimable impacts from the application of AEIFRS.

The accounting policies in this statement are generally consistent with the requirements of AAS. While the scope for financial reporting recommended in AAS 31 is the whole of government (that is, the Australian Government public sector), in accordance with the *Charter of Budget Honesty Act 1998*, the presentation covers the general government sector only. This statement includes notes showing disaggregated information.

AAS 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 (the states), and appropriated to the states. Therefore, accrued GST revenues and associated payments to the states are not recorded in the financial statements.

Note 2: Impacts of Australian Equivalents to International Financial Reporting Standards

The Financial Reporting Council has issued a strategic direction requiring reporting entities in Australia to adopt international accounting standards for reporting periods beginning on or after 1 January 2005. This will involve replacing relevant existing standards with Australian Equivalents to International Financial Reporting Standards (AEIFRS).

The Australian Accounting Standards Board (AASB) has issued the full suite of standards that will apply under AEIFRS including AAS 31 *Financial Reporting by Governments*.

Material estimated impacts on and movements in these financial statements, as if prepared under AEIFRS, are detailed below.[1] The impacts are largely the result of estimating the impact of applying AASB 116 *Property, Plant and Equipment*, AASB 119 *Employee Benefits*, AASB 138 *Intangible Assets*, AASB 139 *Financial Instruments: Recognition and Measurement*, and AASB 140 *Investment Properties*.

The estimated impacts on the Statement of Financial Performance arising from the application of AEIFRS suggest positive impacts to the operating result of $435 million in 2005-06, $320 million in 2006-07, $327 million in 2007-08, and $218 million in 2008-09.

The estimated impacts on the Statement of Financial Position arising from the application of AEIFRS to net assets indicate a negative movement in net assets of $2.93 billion in 2005-06, reducing to a negative movement of $2.15 billion by 2008-09.

There are no cash flow impacts arising from the application of AEIFRS.

The material components of the impacts on these statements are disclosed below.

AASB 116 *Property, Plant and Equipment* requires that the cost of an item of property, plant or equipment include an estimate of the costs of dismantling and removing the asset, and restoring the site on which the asset was situated. AASB 116 requires these costs to be capitalised into the value of the respective assets and an associated provision established.

The yearly impacts on depreciation, borrowing costs and suppliers expenses resulting from applying AASB 116 are a decrease to operating results of $36.1 million in 2005-06, $30.2 million in 2006-07, $26.7 million in 2007-08 and $25.8 million in 2008-09. The cumulative impact on land and buildings, infrastructure, plant and equipment, and provisions result in a negative movement in net assets of $26.2 million in 2005-06, $14.2 million in 2006-07, $13.7 million in 2007-08 and $15.3 million in 2008-09.

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1 These impacts do not include those relating to the Department of Defence, as reliable estimates were not available for the preparation of the 2005-06 Budget estimates.

AASB 119 *Employee Benefits* will require changes in the measurement and recognition of employee annual leave entitlements and superannuation benefits.

The yearly impacts on employee expenses and borrowing costs of applying AASB 119 result in an increase to operating results of $58 million in 2005-06, $2 million in 2006-07, $55 million in 2007-08 and $56 million in 2008-09. The cumulative impact on employee provisions results in a negative movement in net assets of $1.03 billion in 2005-06, $1.03 billion in 2006-07, $0.98 billion in 2007-08 and $0.92 billion in 2008-09.

AASB 138 *Intangible Assets* does not permit intangibles to be measured at valuation unless there is an active market for such an asset. Where intangibles are recorded at valuation, Australian Government entities will derecognise the valuation component of the carrying amount of these assets on adoption of the AEIFRS. These impacts mainly relate to internally developed software.

The yearly impacts on depreciation and amortisation expense of applying AASB 138, result in an increase to operating results of $13 million in 2005-06, $10 million in 2006-07, $8 million in 2007-08 and $7 million in 2008-09. The cumulative impacts on intangible assets result in a negative movement in net assets of $49 million in 2005-06, $39 million in 2006-07, $31 million in 2007-08 and $23 million in 2008-09.

AASB 139 *Financial Instruments: Recognition and Measurement* states that when a financial asset or financial liability is recognised initially, an entity shall measure it at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, *transaction costs* that are directly attributable to the acquisition or issue of the financial asset or financial liability.

The yearly impacts on gains of applying AASB 139 increases operating results by $371 million in 2005-06, $303 million in 2006-07, $257 million in 2007-08 and $148 million in 2008-09. The cumulative impacts on Government securities and payables result in a negative movement in net assets of $2.04 billion in 2005-06, $1.68 billion in 2006-07, $1.39 billion in 2007-08 and $1.22 billion in 2008-09.

AASB 140 *Investment Property* requires investment properties to be separately reported, with all movements to the assets fair value recognised in the operating result. Investment properties held at fair value will not be depreciated.

The yearly impacts on gains and depreciation expense of applying AASB 140 increases operating results by $34 million in 2005-06, $36 million in 2006-07, $37 million in 2007-08 and $37 million in 2008-09. The cumulative impacts on land and buildings and asset reserves result in a negative movement in net assets of $205 million in 2005-06, $234 million in 2006-07, $263 million in 2007-08 and $293 million in 2008-09.

Note 3: Reconciliation of cash

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Operating result (revenues less expenses)	**2,554**	**8,794**	**18,108**	**17,770**	**18,685**
less **Revenues not providing cash**					
Foreign exchange gains	0	0	0	0	0
Gains from asset sales programme	0	0	9,439	9,421	9,472
Gains from sale of assets	53	31	4	13	8
Other	1,005	891	812	778	690
Total revenues not providing cash	**1,058**	**922**	**10,256**	**10,212**	**10,170**
plus **Expenses not requiring cash**					
Increase/(decrease) in employee entitlements	3,536	3,616	3,330	3,357	3,358
Depreciation/amortisation expense	4,409	4,272	4,418	4,575	4,665
Provision for bad and doubtful debts	384	486	556	610	648
Provision for diminution in value of assets	837	96	76	56	53
Losses from asset sales programme	0	0	0	0	0
Losses from sale of assets	0	0	0	0	0
Foreign exchange losses	384	0	0	0	0
Other	3	-54	15	31	-13
Total expenses not requiring cash	**9,553**	**8,417**	**8,395**	**8,630**	**8,711**
plus **Cash provided by working capital items**					
Decrease in inventories	0	0	0	0	0
Decrease in receivables	0	0	0	0	0
Decrease in other financial assets	0	0	0	46	10
Decrease in other non-financial assets	329	321	29	0	0
Increase in benefits subsidies and grants payable	3,921	1,220	587	987	1,001
Increase in suppliers' liabilities	0	8	0	0	0
Increase in other provisions and payables	289	0	231	20	8
Total cash provided by working capital items	**4,539**	**1,548**	**847**	**1,052**	**1,020**
less **Cash used by working capital items**					
Increase in inventories	373	164	351	195	199
Increase in receivables	670	769	1,424	1,577	1,759
Increase in other financial assets	51	30	23	0	0
Increase in other non-financial assets	0	0	0	10	1
Decrease in benefits subsidies and grants payable	0	122	59	48	0
Decrease in other provisions and payables	0	1,170	0	0	0
Decrease in suppliers' liabilities	162	0	25	1	0
Total cash used by working capital items	**1,255**	**2,254**	**1,882**	**1,830**	**1,959**
equals *Net cash from/(to) operating activities*	14,333	15,583	15,212	15,410	16,287
plus Net cash from/(to) investing activities	-13,818	-14,802	-15,191	-17,758	-15,976
Net cash from operating activities and investment	**515**	**781**	**21**	**-2,348**	**311**
plus Net cash from/(to) financing activities	-1,178	-1,420	150	2,099	-379
equals Net (decrease)/increase in cash	**-663**	**-639**	**171**	**-249**	**-67**

Note 3(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		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Total general government sector cash (Statement 10)	927	288	459	210	143
less CAC Agency cash balances	859	202	220	167	120
plus Special public monies	81	81	82	82	82
Balance of Consolidated Revenue Fund at 30 June	**149**	**167**	**321**	**125**	**105**

Further information on the Consolidated Revenue Fund is included in Budget Paper No. 4, *Agency Resourcing 2005-06.*

Note 4: Income taxation revenue

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Individuals and other witholding tax					
Gross income tax withholding	97,990	101,140	106,780	114,300	122,430
Gross other individuals	23,640	25,440	25,990	27,180	28,960
less Refunds	13,700	15,000	15,810	16,580	17,830
Total individuals and other witholding tax	107,930	111,580	116,960	124,900	133,560
Companies	40,610	48,040	50,140	50,780	52,360
Superannuation funds					
Contributions and earnings	5,090	5,070	5,380	5,770	6,220
Surcharge	1,290	1,240	350	210	270
Total superannuation funds	6,380	6,310	5,730	5,980	6,490
Petroleum resource rent tax	1,460	1,350	1,630	1,770	1,520
Total income taxation revenue	**156,380**	**167,280**	**174,460**	**183,430**	**193,930**

Note 5: Indirect taxation revenue

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Excise duty					
Petroleum and other fuel products	13,620	13,980	14,270	14,590	14,840
Crude oil	650	620	580	580	580
Other excise	7,740	7,890	8,000	8,120	8,250
Total excise duty revenue	22,010	22,490	22,850	23,290	23,670
Customs duty revenue	5,714	5,071	5,062	5,322	5,592
Other indirect tax revenue	1,180	1,230	1,340	1,420	1,500
GST	36,300	38,000	40,060	42,270	44,520
less transfers to states and territories in relation to GST revenue	36,300	38,000	40,060	42,270	44,520
GST revenue	0	0	0	0	0
Mirror taxes	347	366	384	402	422
less transfers to states and territories in relation to mirror tax revenue	347	366	384	402	422
Mirror tax revenue	0	0	0	0	0
Indirect tax revenue	**28,904**	**28,791**	**29,252**	**30,032**	**30,762**

Note 6: Interest and dividend revenue

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Interest					
Interest from other governments					
State and Territory debt	29	17	15	14	10
Housing agreements	174	170	166	162	158
Total interest from other governments	**203**	**187**	**181**	**176**	**168**
Interest from other sources					
Swap interest	2,165	2,327	2,250	1,869	1,387
Advances	17	3	3	3	3
Deposits	0	0	0	0	0
Bills receivable	6	6	6	6	5
Bank deposits	188	187	185	180	182
Indexation of HECS receivable and other student loans	319	370	387	431	484
Other	828	1,248	2,092	3,202	4,183
Total interest from other sources	**3,524**	**4,140**	**4,922**	**5,690**	**6,243**
Total interest	**3,727**	**4,327**	**5,103**	**5,866**	**6,411**
Dividends					
Dividends from controlled entities	3,126	3,293	2,911	2,337	1,833
Other dividends	19	19	41	20	20
Total dividends	**3,146**	**3,312**	**2,952**	**2,357**	**1,852**
Total interest and dividend revenue	**6,873**	**7,639**	**8,055**	**8,222**	**8,264**

Note 7: Other sources of non-taxation revenue

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Assets now recognised	623	124	92	58	58
Gains on derivative financial instruments	0	371	303	257	148
Industry contributions	290	264	245	228	208
International Monetary Fund related revenue	38	41	41	41	41
Royalties	783	828	745	771	811
Seigniorage	106	112	102	106	106
Other	2,005	1,913	1,884	1,898	1,909
Total other sources of non-taxation revenue	**3,845**	**3,652**	**3,412**	**3,359**	**3,282**

Note 8: Employee expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Salaries and wages(a)	11,922	12,617	12,828	13,164	13,668
Leave and other entitlements	1,404	1,425	1,447	1,512	1,534
Separations and redundancies	75	65	65	67	68
Workers compensation premiums	0	0	0	0	7
Other (including superannuation)	9,509	9,170	9,108	9,447	9,734
Total employee expenses	**22,911**	**23,277**	**23,449**	**24,190**	**25,010**

(a) Salaries and wages do not include superannuation.

Note 9: Suppliers expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Supply of goods and services	14,738	15,721	15,664	15,986	15,324
Operating lease rental expenses	1,687	1,699	1,716	1,749	1,710
Other	423	474	588	585	558
Total supplier expenses	**16,848**	**17,893**	**17,968**	**18,321**	**17,592**

Note 10: Depreciation and amortisation expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Depreciation					
Specialist military equipment	2,517	2,132	2,166	2,234	2,304
Buildings	532	591	603	623	640
Heritage and cultural assets	43	44	44	46	47
Other infrastructure, plant and equipment	986	1,133	1,189	1,238	1,266
Total depreciation	**4,078**	**3,899**	**4,002**	**4,141**	**4,257**
Total amortisation	**331**	**373**	**416**	**434**	**408**
Total depreciation and amortisation expenses	**4,409**	**4,272**	**4,418**	**4,575**	**4,665**

Note 11: Other goods and services expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Health care payments	4,238	4,574	4,847	5,155	5,452
Development cooperation program	1,312	1,353	1,369	1,368	1,425
Other	1,528	1,552	1,831	1,865	1,853
Total other goods and services expenses	**7,078**	**7,479**	**8,046**	**8,388**	**8,730**

Note 12: Grants expenses

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
State and territory governments	25,320	27,319	27,474	28,543	29,135
Non-profit organisations	1,541	1,498	1,599	1,651	1,674
Overseas	1,040	531	438	854	832
Private sector	1,423	1,735	1,290	1,146	1,102
Local governments	318	444	412	391	389
Multi-jurisdictional sector	5,347	5,789	6,002	6,172	6,318
Other	4,485	5,098	5,755	6,197	5,684
Total grant expenses	**39,474**	**42,414**	**42,970**	**44,954**	**45,134**

Note 13: Receivables

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Taxes receivable	11,519	12,890	14,811	16,707	18,758
Advances and loans	11,879	12,429	13,270	14,127	14,809
Other receivables	6,431	6,559	6,901	7,626	8,620
Total receivables	**29,829**	**31,878**	**34,982**	**38,461**	**42,187**

Note 14: Total non-financial assets

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Land and buildings					
Land	4,863	5,161	5,119	5,027	4,973
Buildings	13,894	14,008	14,263	14,428	14,536
Total land and buildings	**18,757**	**19,169**	**19,382**	**19,455**	**19,509**
Infrastructure					
Specialist military equipment	30,988	32,195	33,753	35,468	37,245
Other	8,411	8,578	8,716	8,546	8,256
Total infrastructure	**39,398**	**40,773**	**42,470**	**44,015**	**45,501**
Intangibles					
Computer software	1,585	1,662	1,624	1,597	1,550
Other	108	96	87	75	61
Total intangibles	**1,693**	**1,758**	**1,711**	**1,672**	**1,610**
Heritage and cultural assets	6,698	6,739	6,766	6,787	6,808
Total heritage and cultural assets	**6,698**	**6,739**	**6,766**	**6,787**	**6,808**
Inventories	5,299	5,570	5,989	6,228	6,463
Total inventories	**5,299**	**5,570**	**5,989**	**6,228**	**6,463**
Other non-financial assets					
Prepayments	1,440	1,160	1,131	1,141	1,142
Other	392	583	496	334	151
Total other non-financial assets	**1,832**	**1,743**	**1,627**	**1,474**	**1,293**
Total non-financial assets	**73,678**	**75,751**	**77,945**	**79,631**	**81,184**

Note 15: Employee and superannuation liabilities

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Superannuation	90,691	95,175	98,375	101,547	104,695
Leave and other entitlements	4,271	4,283	4,293	4,275	4,337
Accrued salaries and wages	117	160	188	219	235
Workers compensation claims	1,484	1,454	1,391	1,391	1,356
Separations and redundancies	34	37	38	38	39
Workers compensation premiums	1,702	1,854	1,962	2,083	2,199
Other	376	427	472	523	573
Total employee and superannuation liabilities	**98,676**	**103,390**	**106,720**	**110,076**	**113,434**

Note 16: Grants payable

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
State and territory governments	4,000	4,273	4,553	4,829	5,092
Non-profit organisations	72	67	67	67	67
Private sector	671	478	282	73	73
Overseas	1,311	1,182	947	1,117	1,305
Local governments	5	5	5	5	5
Other	3,782	4,031	4,166	4,274	4,349
Total grants payable	**9,842**	**10,035**	**10,019**	**10,365**	**10,891**

Note 17: Net asset movements

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Opening net assets	**-42,207**	**-39,797**	**-34,579**	**-16,357**	**1,435**
Operating result after extraordinary items	2,554	8,794	18,108	17,770	18,685
Asset revaluation reserve	187	-24	107	21	65
Other movements	-330	-3,553	8	0	-13
Closing net assets	**-39,797**	**-34,579**	**-16,357**	**1,435**	**20,171**

Note 18: Taxation receipts — cash

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Total taxation receipts	222,030	235,469	244,499	256,449	269,747
less payments to states and territories in relation to GST revenue	35,550	37,340	39,200	41,320	43,480
less payments to states and territories in relation to mirror tax revenue	347	366	384	402	422
Taxation receipts	**186,133**	**197,763**	**204,915**	**214,727**	**225,845**

APPENDIX A: ADDITIONAL AGENCY STATISTICS

Table A1: General government expenses by agency

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	1,973	1,901	1,718	1,574	1,340
Grains Research and Development Corporation	127	132	131	131	112
Dairy Structural Adjustment Fund	56	45	35	24	15
Total	**2,156**	**2,078**	**1,884**	**1,729**	**1,467**
Attorney-General's					
Attorney-General's Department	580	631	665	708	696
Australian Customs Service	936	981	999	1,003	1,014
Australian Federal Police	865	1,018	1,011	1,009	831
Family Court of Australia	130	137	138	139	140
High Court of Australia	12	14	14	14	14
Total	**2,523**	**2,782**	**2,828**	**2,873**	**2,696**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	747	800	647	577	524
Australian Broadcasting Authority (Administered)	17	18	18	18	18
Australian Broadcasting Corporation	1011	1016	1004	1018	1016
Australian Communications Authority (Administered)	59	61	60	60	60
Australian Sports Commission	167	187	200	188	170
National Archives of Australia	70	68	68	68	68
National Gallery of Australia	48	46	47	48	49
National Library of Australia	67	68	68	69	69
National Museum of Australia	44	44	44	45	46
Special Broadcasting Service Corporation	212	234	228	228	233
Total	**2,442**	**2,543**	**2,385**	**2,319**	**2,252**
Defence					
Department of Defence	19,108	19,034	18,956	19,890	20,340
Defence Material Organisation	0	7,125	7,133	7,641	7,921
Defence Housing Authority	719	748	858	915	926
Department of Veterans' Affairs	10,569	10,967	11,285	11,624	11,908
Australian War Memorial	38	39	40	39	41
Total	**30,434**	**37,914**	**38,271**	**40,109**	**41,135**
Education, Science and Training					
Department of Education, Science and Training	17,297	19,590	20,670	21,643	22,316
Australian National Training Authority	763	0	0	0	0
Australian Research Council	574	581	595	596	611
Australian Nuclear Science and Technology Organisation	154	158	172	166	181
Commonwealth Scientific and Industrial Research Organisation	909	963	1,025	1,071	1,077
Total	**19,696**	**21,292**	**22,462**	**23,476**	**24,184**

Table A1: General government expenses by agency (continued)

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Employment and Workplace Relations					
Department of Employment and Workplace Relations	17,549	25,730	27,142	28,424	29,254
Comcare	332	244	290	303	316
Total	**17,881**	**25,974**	**27,432**	**28,727**	**29,570**
Environment and Heritage					
Department of Environment and Heritage	784	832	892	858	454
Bureau of Meteorology	208	224	231	237	239
Total	**992**	**1,056**	**1,123**	**1,094**	**693**
Family and Community Services					
Department of Family and Community Services	51,467	44,498	46,906	48,893	51,404
Total	**51,467**	**44,498**	**46,906**	**48,893**	**51,404**
Finance and Administration					
Department of Finance and Administration	6,327	5,746	6,129	6,243	6,297
Australian Electoral Commission	228	106	110	228	109
Future Fund Management Agency	0	6	8	8	8
Department of Human Services	758	1,403	1,574	1,601	1,615
Centrelink	2,259	2,306	2,332	2,435	2,492
Health Insurance Commission	594	567	576	586	599
Total	**10,165**	**10,135**	**10,729**	**11,101**	**11,121**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	1,009	957	923	988	923
AusAID	2,214	1,749	1,668	2,083	2,119
Australian Trade Commission	330	373	355	347	348
Total	**3,553**	**3,079**	**2,946**	**3,418**	**3,389**
Health and Ageing					
Department of Health and Ageing	36,776	39,148	40,908	43,072	45,078
National Blood Authority	554	578	577	578	578
Total	**37,331**	**39,726**	**41,485**	**43,650**	**45,657**
Immigration and Multicultural and Indigenous Affairs					
Department of Immigration and Multicultural and Indigenous Affairs	2,192	1,802	1,813	1,828	1,871
Aboriginal and Torres Strait Islanders Land Fund	0	0	0	0	0
Aboriginal and Torres Strait Islander Services	0	0	0	0	0
Total	**2,192**	**1,802**	**1,813**	**1,828**	**1,871**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	1,872	2,071	1,862	1,804	1,814
Tourism Australia	165	163	159	162	114
Total	**2,038**	**2,235**	**2,021**	**1,966**	**1,928**
Parliament					
Department of Parliamentary Services	158	160	163	165	167
Total	**158**	**160**	**163**	**165**	**167**
Prime Minister and Cabinet					
Department of Prime Minister and Cabinet	88	99	119	115	72
National Water Commission	11	326	570	560	201
Total	**99**	**426**	**690**	**675**	**273**

Table A1: General government expenses by agency (continued)

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Transport and Regional Services					
Department of Transport and Regional Services	3,955	4,197	4,438	4,586	4,491
Civil Aviation Safety Authority	114	118	118	120	123
National Capital Authority	31	28	29	29	30
Total	**4,100**	**4,343**	**4,585**	**4,735**	**4,644**
Treasury					
Department of the Treasury(a)	1,159	1,137	217	203	29
Australian Bureau of Statistics	288	338	431	316	297
Australian Securities and Investment Commission	259	264	247	251	251
Australian Taxation Office(a)	14,578	12,026	12,143	12,348	12,985
Australian Office of Financial Management	5,976	6,068	5,694	5,325	4,681
Total	**22,260**	**19,833**	**18,732**	**18,443**	**18,242**
Small agencies	**2,875**	**3,082**	**3,095**	**3,114**	**3,131**
Whole of government and inter-agency amounts(b)	**-8,502**	**-13,881**	**-10,476**	**-8,768**	**-3,924**
Total expenses	**203,858**	**209,074**	**219,074**	**229,549**	**239,902**

(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 and appropriated to the states and territories by the Department of the Treasury as agent for the states and territories.

(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		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	515	501	485	480	468
Grains Research and Development Corporation	127	132	131	131	112
Dairy Structural Adjustment Fund	0	0	0	0	0
Total	**642**	**632**	**616**	**611**	**580**
Attorney-General's					
Attorney-General's Department	202	188	180	170	159
Australian Customs Service	935	978	996	1,000	1,011
Australian Federal Police	865	1,018	1,011	1,009	831
Family Court of Australia	130	137	138	139	140
High Court of Australia	12	14	14	14	14
Total	**2,145**	**2,336**	**2,340**	**2,332**	**2,156**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	121	120	121	119	120
Australian Broadcasting Authority (Administered)	17	18	18	18	18
Australian Broadcasting Corporation	925	930	918	932	930
Australian Communications Authority (Administered)	59	61	60	60	60
Australian Sports Commission	167	187	200	188	170
National Archives of Australia	70	68	68	68	68
National Gallery of Australia	48	46	47	48	49
National Library of Australia	67	68	68	69	69
National Museum of Australia	44	44	44	45	46
Special Broadcasting Service Corporation	212	234	228	228	233
Total	**1,730**	**1,777**	**1,773**	**1,775**	**1,762**
Defence					
Department of Defence	16,670	16,495	16,417	17,250	17,701
Defence Material Organisation	0	7,125	7,133	7,641	7,921
Defence Housing Authority	719	748	858	915	926
Department of Veterans' Affairs	329	324	321	314	307
Australian War Memorial	38	39	40	39	41
Total	**17,756**	**24,732**	**24,768**	**26,159**	**26,895**
Education, Science and Training					
Department of Education, Science and Training	367	431	434	436	434
Australian National Training Authority	15	0	0	0	0
Australian Research Council	14	15	15	15	16
Australian Nuclear Science and Technology Organisation	154	158	172	166	181
Commonwealth Scientific and Industrial Research Organisation	909	963	1,025	1,071	1,077
Total	**1,459**	**1,567**	**1,646**	**1,688**	**1,707**

Table A2: Departmental expenses by agency (continued)

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Employment and Workplace Relations					
Department of Employment and Workplace Relations	1,061	1,463	1,521	1,618	1,617
Comcare	332	244	290	303	316
Total	**1,393**	**1,706**	**1,812**	**1,920**	**1,933**
Environment and Heritage					
Department of Environment and Heritage	335	351	344	325	256
Bureau of Meteorology	208	224	231	237	239
Total	**543**	**575**	**574**	**562**	**495**
Family and Community Services					
Department of Family and Community Services	2,348	1,470	1,443	1,434	1,472
Total	**2,348**	**1,470**	**1,443**	**1,434**	**1,472**
Finance and Administration					
Department of Finance and Administration	372	426	592	576	552
Australian Electoral Commission	184	106	110	181	109
Future Fund Management Agency	0	6	8	8	8
Department of Human Services	252	466	482	491	503
Centrelink	2,259	2,306	2,332	2,435	2,492
Health Insurance Commission	594	567	576	586	599
Total	**3,660**	**3,878**	**4,101**	**4,277**	**4,264**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	726	708	703	768	704
AusAID	75	79	75	75	75
Australian Trade Commission	194	203	195	196	197
Total	**995**	**990**	**972**	**1,040**	**976**
Health and Ageing					
Department of Health and Ageing	568	543	528	528	533
National Blood Authority	8	10	10	10	9
Total	**576**	**553**	**537**	**537**	**542**
Immigration and Multicultural and Indigenous Affairs					
Department of Immigration and Multicultural and Indigenous Affairs	1,016	1,064	1,088	1,119	1,155
Aboriginal and Torres Strait Islanders Land Fund	0	0	0	0	0
Aboriginal and Torres Strait Islander Services	0	0	0	0	0
Total	**1,016**	**1,064**	**1,088**	**1,119**	**1,155**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	312	298	285	280	271
Tourism Australia	165	163	159	162	114
Total	**477**	**461**	**444**	**441**	**385**
Parliament					
Department of Parliamentary Services	118	120	122	124	126
Total	**118**	**120**	**122**	**124**	**126**
Prime Minister and Cabinet					
Department of Prime Minister and Cabinet	62	87	107	103	60
National Water Commission	5	10	10	10	10
Total	**67**	**98**	**118**	**113**	**70**

Table A2: Departmental expenses by agency (continued)

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Transport and Regional Services					
Department of Transport and Regional Services	185	207	206	203	204
Civil Aviation Safety Authority	114	118	118	120	123
National Capital Authority	20	20	20	20	20
Total	**319**	**344**	**344**	**344**	**348**
Treasury					
Department of the Treasury	174	184	177	170	172
Australian Bureau of Statistics	288	338	431	316	297
Australian Securities and Investment Commission	214	222	205	207	207
Australian Taxation Office	2,445	2,502	2,484	2,502	2,536
Australian Office of Financial Management	8	8	8	8	8
Total	**3,129**	**3,254**	**3,306**	**3,203**	**3,219**
Small agencies	**2,875**	**3,082**	**3,095**	**3,114**	**3,131**
Whole of government and inter-agency amounts(a)	**0**	**-43**	**-227**	**-506**	**-577**
Total departmental expenses	**41,248**	**48,595**	**48,872**	**50,289**	**50,638**

(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		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	-6.1	-0.2	-8.8	0.0	0.0
Grains Research and Development Corporation	-0.2	-0.1	-0.1	0.0	-0.1
Dairy Structural Adjustment Fund	0.0	0.0	0.0	0.0	0.0
Total	**-6.3**	**-0.3**	**-8.9**	**0.0**	**-0.1**
Attorney-General's					
Attorney-General's Department	5.9	13.1	13.0	-4.4	-4.8
Australian Customs Service	52.7	5.7	4.7	-3.3	-9.1
Australian Federal Police	82.1	42.2	-11.7	-13.4	-1.0
Family Court of Australia	2.0	-0.6	-0.4	-0.4	-0.4
High Court of Australia	1.6	-0.3	-0.5	-0.5	-0.6
Total	**144.3**	**60.0**	**5.1**	**-22.0**	**-15.9**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	-0.8	-1.9	-1.8	47.0	-4.0
Australian Broadcasting Authority (Administered)	-0.9	-0.8	-0.8	-0.2	-0.4
Australian Broadcasting Corporation	-31.9	-11.0	0.0	0.0	0.0
Australian Communications Authority (Administered)	-2.0	-1.7	-3.3	-1.1	0.3
Australian Sports Commission	19.2	23.0	6.8	-8.0	-7.2
National Archives of Australia	265.0	27.6	26.5	26.9	26.2
National Gallery of Australia	-3.6	12.1	14.2	-5.5	-5.2
National Library of Australia	-2.8	11.0	-6.1	-6.2	-6.7
National Museum of Australia	5.8	2.0	-2.5	-0.7	-4.8
Special Broadcasting Service Corporation	-0.4	1.4	-1.2	-1.5	-0.5
Total	**247.7**	**61.7**	**31.8**	**50.8**	**-2.3**
Defence					
Department of Defence	243.9	-4,427.1	1,624.1	1,726.1	2,133.9
Defence Material Organisation	0.0	5,669.4	172.0	131.7	143.0
Defence Housing Authority	117.4	152.3	143.8	22.1	-32.4
Department of Veterans' Affairs	2.9	13.2	4.2	0.2	0.6
Australian War Memorial	4.6	9.4	5.0	0.8	-1.2
Total	**368.8**	**1,417.2**	**1,949.1**	**1,880.9**	**2,244.0**
Education, Science and Training					
Department of Education, Science and Training	6.2	1.5	0.7	4.2	-2.0
Australian National Training Authority	0.0	-1.0	0.0	0.0	0.0
Australian Research Council	-0.8	3.4	0.1	-0.5	-0.5
Australian Nuclear Science and Technology Organisation	85.5	78.3	5.4	0.2	1.0
Commonwealth Scientific and Industrial Research Organisation	9.1	5.3	6.2	36.8	6.7
Total	**99.9**	**87.5**	**12.4**	**40.8**	**5.2**

Table A3: Net capital investment by agency (continued)

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Employment and Workplace Relations					
Department of Employment and Workplace Relations	17.2	39.6	6.3	1.8	-11.9
Comcare	0.4	-0.1	0.0	0.0	0.0
Total	**17.5**	**39.5**	**6.3**	**1.8**	**-11.9**
Environment and Heritage					
Department of Environment and Heritage	-4.9	-2.7	-5.3	-11.5	-11.7
Bureau of Meteorology	15.1	8.2	11.7	15.0	5.2
Total	**10.2**	**5.5**	**6.5**	**3.5**	**-6.4**
Family and Community Services					
Department of Family and Community Services	-33.2	2.5	1.3	1.7	1.6
Total	**-33.2**	**2.5**	**1.3**	**1.7**	**1.6**
Finance and Administration					
Department of Finance and Administration	74.1	230.0	-129.2	29.5	-64.6
Australian Electoral Commission	-4.9	1.0	3.0	-1.1	-0.2
Future Fund Management Agency	0.0	1.0	0.0	0.0	0.0
Department of Human Services	50.1	-4.6	1.7	-3.7	-10.3
Centrelink	49.5	28.1	19.9	-6.6	-12.1
Health Insurance Commission	14.9	0.8	-1.9	-3.1	-5.1
Total	**183.8**	**256.3**	**-106.6**	**15.1**	**-92.3**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	-36.3	221.1	212.9	43.1	-18.7
AusAID	5.1	1.5	5.3	-2.4	-2.9
Australian Trade Commission	0.1	8.2	6.6	3.5	-1.5
Total	**-31.1**	**230.8**	**224.9**	**44.3**	**-23.1**
Health and Ageing					
Department of Health and Ageing	-48.2	-32.6	-35.5	-9.3	-7.5
National Blood Authority	1.2	1.9	0.2	-0.4	-0.4
Total	**-47.0**	**-30.7**	**-35.3**	**-9.7**	**-7.9**
Immigration and Multicultural and Indigenous Affairs					
Department of Immigration and Multicultural and Indigenous Affairs	42.5	3.9	280.8	-32.7	69.5
Aboriginal and Torres Strait Islanders Land Fund	0.0	0.0	0.0	0.0	0.0
Aboriginal and Torres Strait Islander Services	-48.1	0.0	0.0	0.0	0.0
Total	**-5.6**	**3.9**	**280.8**	**-32.7**	**69.5**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	16.4	-4.1	1.5	2.2	1.9
Tourism Australia	5.1	-0.9	-0.7	-2.7	-1.9
Total	**21.5**	**-5.0**	**0.8**	**-0.5**	**0.0**
Parliament					
Department of Parliamentary Services	-4.2	-27.9	-33.9	-33.7	-34.4
Total	**-4.2**	**-27.9**	**-33.9**	**-33.7**	**-34.4**
Prime Minister and Cabinet					
Department of Prime Minister and Cabinet	1.8	8.2	12.6	-5.2	-1.7
National Water Commission	2.0	-0.3	-0.3	-0.3	-0.3
Total	**3.8**	**7.9**	**12.3**	**-5.5**	**-2.0**

Table A3: Net capital investment by agency (continued)

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Transport and Regional Services					
Department of Transport and Regional Services	15.6	60.7	-1.9	-6.9	-8.4
Civil Aviation Safety Authority	14.0	4.5	-2.4	-3.8	-5.9
National Capital Authority	1.7	6.3	3.4	0.7	1.3
Total	**31.4**	**71.6**	**-0.9**	**-9.9**	**-13.0**
Treasury					
Department of the Treasury	-154.1	-217.6	9.8	6.4	1.2
Australian Bureau of Statistics	0.0	9.9	-5.0	-0.6	-9.4
Australian Securities and Investment Commission	1.9	-1.1	-4.0	-2.0	-0.3
Australian Taxation Office	19.7	37.0	28.3	16.3	8.1
Australian Office of Financial Management	-0.8	-0.8	1.2	-0.6	-0.6
Total	**-133.3**	**-172.6**	**30.3**	**19.6**	**-1.1**
Small agencies	**42.8**	**45.6**	**54.1**	**50.6**	**57.8**
Whole of government and inter-agency amounts(a)	**-1.6**	**19.7**	**-236.8**	**-308.6**	**-614.8**
Total net capital investment	**909.4**	**2,073.1**	**2,193.3**	**1,686.1**	**1,553.0**

(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		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	6	0	0	0	0
Grains Research and Development Corporation	0	0	0	0	0
Dairy Structural Adjustment Fund	0	0	0	0	0
Total	**6**	**0**	**0**	**0**	**0**
Attorney-General's					
Attorney-General's Department	9	13	9	0	0
Australian Customs Service	42	16	17	12	10
Australian Federal Police	30	44	14	12	11
Family Court of Australia	2	0	0	0	0
High Court of Australia	0	0	0	0	0
Total	**83**	**73**	**40**	**24**	**21**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	0	0	0	0	0
Australian Broadcasting Authority (Administered)	0	3	0	0	0
Australian Broadcasting Corporation	0	0	0	0	0
Australian Communications Authority (Administered)	0	28	0	0	0
Australian Sports Commission	12	21	11	0	0
National Archives of Australia	0	0	0	0	0
National Gallery of Australia	4	4	22	4	4
National Library of Australia	4	7	1	1	1
National Museum of Australia	1	1	3	5	1
Special Broadcasting Service Corporation	6	6	5	4	3
Total	**26**	**70**	**42**	**14**	**9**
Defence					
Department of Defence	393	1,121	1,512	1,612	2,018
Defence Material Organisation	0	0	0	0	0
Defence Housing Authority	0	125	0	0	0
Department of Veterans' Affairs	2	6	1	1	1
Australian War Memorial	7	3	0	0	0
Total	**402**	**1,255**	**1,513**	**1,613**	**2,019**
Education, Science and Training					
Department of Education, Science and Training	8	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	43	20	0	0	0
Commonwealth Scientific and Industrial Research Organisation	0	0	0	0	0
Total	**51**	**20**	**0**	**0**	**0**

Table A4: Capital appropriations by portfolio (continued)

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Employment and Workplace Relations					
Department of Employment and Workplace Relations	26	46	13	6	0
Comcare	0	0	0	0	0
Total	**26**	**46**	**13**	**6**	**0**
Environment and Heritage					
Department of Environment and Heritage	0	5	2	0	0
Bureau of Meteorology	9	13	17	17	5
Total	**9**	**18**	**19**	**17**	**5**
Family and Community Services					
Department of Family and Community Services	1	1	0	0	0
Total	**1**	**1**	**0**	**0**	**0**
Finance and Administration					
Department of Finance and Administration	988	1,044	965	880	958
Australian Electoral Commission	2	2	1	1	2
Future Fund Management Agency	0	16,138	0	0	0
Department of Human Services	0	0	0	0	0
Centrelink	38	54	26	15	0
Health Insurance Commission	20	4	2	1	0
Total	**1,048**	**17,242**	**994**	**898**	**960**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	82	77	71	87	1
AusAID	97	36	29	16	8
Australian Trade Commission	6	9	8	5	0
Total	**185**	**122**	**108**	**107**	**9**
Health and Ageing					
Department of Health and Ageing	60	58	56	48	48
National Blood Authority	0	0	0	0	0
Total	**60**	**58**	**57**	**48**	**48**
Immigration and Multicultural and Indigenous Affairs					
Department of Immigration and Multicultural and Indigenous Affairs	60	31	33	25	42
Aboriginal and Torres Strait Islanders Land Fund	0	0	0	0	0
Aboriginal and Torres Strait Islander Services	0	0	0	0	0
Total	**60**	**31**	**33**	**25**	**42**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	172	26	13	34	8
Tourism Australia	1	0	0	0	0
Total	**173**	**26**	**13**	**34**	**8**
Parliament					
Department of Parliamentary Services	12	0	0	0	0
Total	**12**	**0**	**0**	**0**	**0**
Prime Minister and Cabinet					
Department of Prime Minister and Cabinet	3	10	18	0	0
National Water Commission	2	0	0	0	0
Total	**5**	**10**	**18**	**0**	**0**

Table A4: Capital appropriations by portfolio (continued)

	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m	$m
Transport and Regional Services					
Department of Transport and Regional Services	99	21	7	6	5
Civil Aviation Safety Authority	0	0	0	0	0
National Capital Authority	2	2	2	2	2
Total	**101**	**23**	**9**	**8**	**7**
Treasury					
Department of the Treasury	347	89	77	57	36
Australian Bureau of Statistics	0	1	1	1	0
Australian Securities and Investment Commission	12	1	0	0	0
Australian Taxation Office	8	0	0	0	0
Australian Office of Financial Management	161,362	142,625	141,575	138,394	140,570
Total	**161,729**	**142,717**	**141,653**	**138,451**	**140,606**
Small agencies	**0**	**0**	**0**	**0**	**0**
Whole of government and inter-agency amounts(a)	**0**	**0**	**0**	**0**	**0**
Total capital appropriations	**163,976**	**161,713**	**144,512**	**141,243**	**143,733**

(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		
	2004-05	2005-06	Change
Agriculture, Fisheries and Forestry			
Department of Agriculture, Fisheries and Forestry	3,832	3,832	0
Australian Fisheries Management Authority	124	124	0
Australian Pesticides and Veterinary Medicines Authority	125	125	0
Australian Wine and Brandy Corporation	54	54	0
Biosecurity Australia	42	100	58
Cotton Research and Development Corporation	11	11	0
Dairy Structural Adjustment Fund	4	4	0
Fisheries Research and Development Corporation	10	10	0
Forest and Wood Products Research and Development Corporation	7	7	0
Grains Research and Development Corporation	50	55	5
Grape and Wine Research and Development Corporation	9	9	0
Land and Water Resources Research and Development Corporation	33	33	0
Rural Industries Research and Development Corporation	17	17	0
Sugar Research and Development Corporation	6	6	0
Wheat Export Authority	12	12	0
Total	**4,336**	**4,399**	**63**
Attorney-General's			
Attorney-General's Department	877	991	114
Administrative Appeals Tribunal	161	161	0
Australian Crime Commission	475	490	15
Australian Customs Service	4,731	4,802	71
Australian Federal Police	4,865	5,191	326
Australian Institute of Criminology	45	42	-3
Australian Law Reform Commission	18	18	0
Australian Security Intelligence Organisation	997	1,244	247
Australian Transaction Reports and Analysis Centre (AUSTRAC)	106	119	13
Criminology Research Council	2	2	0
CrimTrac	52	68	16
Family Court of Australia	680	680	0
Federal Court of Australia	335	338	3
Federal Magistrates Service	114	127	13
High Court of Australia	86	93	7
Human Rights and Equal Opportunity Commission	97	89	-8
Insolvency and Trustee Service Australia	260	260	0
National Native Title Tribunal	255	240	-15
Office of Film and Literature Classification	51	51	0
Office of Parliamentary Counsel	40	45	5
Office of the Director of Public Prosecutions	468	472	4
Office of the Privacy Commissioner	35	35	0
Total	**14,750**	**15,558**	**808**

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2004-05	2005-06	Change
Communication, Information Technology and the Arts			
Department of Communications, Information Technology and the Arts	770	803	33
Australia Business Arts Foundation	28	30	2
Australia Council	135	135	0
Australian Broadcasting Authority	112	112	0
Australian Broadcasting Corporation	4,200	4,200	0
Australian Communications Authority	410	399	-11
Australian Film Commission	275	278	3
Australian Film Television and Radio School	148	158	10
Australian Government Information Management Office	33	0	-33
Australian National Maritime Museum	100	105	5
Australian Sports Commission	551	628	77
Australian Sports Drug Agency	38	47	9
Bundanon Trust	12	14	2
Film Australia	53	55	2
National Archives of Australia	420	452	32
National Gallery of Australia	230	228	-2
National Library of Australia	451	449	-2
National Museum of Australia	220	225	5
Netalert	4	4	0
Special Broadcasting Service	798	790	-8
Total	**8,988**	**9,111**	**124**
Defence			
Department of Defence	17,973	13,282	-4,691
Military Reserves	20,250	20,150	-100
Permanent Military	52,008	52,000	-8
Defence Housing Authority	750	750	0
Defence Materiel Organisation	0	4,448	4,448
Department of Veterans' Affairs	2,487	2,468	-19
Australian War Memorial	278	282	4
Total	**93,746**	**93,380**	**-366**
Education, Science and Training			
Department of Education, Science and Training	1,835	2,000	165
Australian Institute of Aboriginal and Torres Strait Islander Studies	108	110	2
Australian Institute of Marine Science	162	168	6
Australian National Training Authority	83	0	-83
Australian Nuclear Science and Technology Organisation	835	838	3
Australian Research Council	64	76	12
Commonwealth Scientific and Industrial Research Organisation	6,016	6,030	14
Total	**9,103**	**9,222**	**119**
Employment and Workplace Relations			
Department of Employment and Workplace Relations	2,735	3,160	425
Australian Industrial Registry	249	257	8
Comcare	333	348	15
Equal Opportunity for Women in the Workplace Agency	21	21	0
Indigenous Business Australia	47	126	79
National Occupation Health and Safety Commission	50	0	-50
Total	**3,435**	**3,912**	**477**

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2004-05	2005-06	Change
Environment and Heritage			
Department of the Environment and Heritage	1,464	1,612	148
Australian Greenhouse Office	58	0	-58
Bureau of Meteorology	1,413	1,355	-58
Director of National Parks	275	275	0
Great Barrier Reef Marine Park Authority	180	179	-1
National Oceans Office	15	0	-15
Office of the Renewable Energy Regulator	10	11	1
Sydney Harbour Federation Trust	46	50	4
Total	**3,461**	**3,482**	**21**
Family and Community Services			
Department of Family and Community Services	1,770	1,770	0
Aboriginal Hostels Limited	385	385	0
Australian Institute of Family Studies	55	55	0
Total	**2,210**	**2,210**	**0**
Finance and Administration			
Department of Finance and Administration	1,056	1,248	192
Australian Electoral Commission	807	775	-32
Commonwealth Grants Commission	48	48	0
Commonwealth Superannuation Administration (ComSuper)	384	384	0
Department of Human Services	4,508	4,613	105
Centrelink	23,400	22,950	-450
Health Insurance Commission	5,150	5,050	-100
Total	**35,353**	**35,068**	**-285**
Foreign Affairs and Trade			
Department of Foreign Affairs and Trade	3,138	3,161	23
AusAID	510	482	-28
Australian Trade Commission	1,056	1,094	38
Australia-Japan Foundation	6	6	0
Australian Centre for International Agricultural Research	62	63	1
Total	**4,772**	**4,806**	**34**
Health and Ageing			
Department of Health and Ageing	3,805	3,927	122
Aged Care Standards and Accreditation Agency	151	191	40
Australian Institute of Health and Welfare	186	192	6
Australian Radiation Protection and Nuclear Safety Agency	122	126	4
Food Standards Australia New Zealand	126	122	-4
General Practice Education and Training Limited	27	29	2
National Blood Authority	34	40	6
National Institute of Clinical Studies Australia Limited	18	22	4
Private Health Insurance Administration Council	13	15	2
Private Health Insurance Ombudsman	8	8	0
Professional Services Review	35	30	-5
Total	**4,525**	**4,702**	**177**
Immigration and Multicultural and Indigenous Affairs			
Department of Immigration and Multicultural and Indigenous Affairs	5,692	5,747	55
Migration Review Tribunal	174	174	0
Refugee Review Tribunal	190	190	0
Indigenous Land Corporation	130	130	0
Torres Strait Regional Authority	50	50	0
Total	**6,236**	**6,291**	**55**

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2004-05	2005-06	Change
Industry Tourism and Resources			
Department of Industry, Tourism and Resources	1,742	1,750	8
Geoscience Australia	626	646	20
IP Australia	775	795	20
National Offshore Petroleum Safety Authority	13	34	21
Tourism Australia	245	245	0
Total	**3,401**	**3,470**	**69**
Parliament			
Department of Parliamentary Services	845	845	0
Department of the House of Representatives	166	166	0
Department of the Senate	169	169	0
Total	**1,180**	**1,180**	**0**
Prime Minister and Cabinet			
Department of the Prime Minister and Cabinet	375	450	75
Australian National Audit Office	290	300	10
Australian Public Service Commission	187	179	-8
National Water Commission	22	52	30
Office of National Assessments	95	125	30
Office of the Commonwealth Ombudsman	102	102	0
Office of the Inspector-General of Intelligence and Security	6	7	1
Office of the Official Secretary to the Governor-General	83	91	8
Total	**1,160**	**1,306**	**146**
Transport and Regional Services			
Department of Transport and Regional Services	1,038	1,192	154
Australian Maritime Safety Authority	237	241	4
Civil Aviation Safety Authority	680	650	-30
National Capital Authority	86	87	1
Total	**2,041**	**2,170**	**129**
Treasury			
Department of the Treasury	890	934	44
Australian Bureau of Statistics	2,652	2,711	59
Australian Competition and Consumer Commission	481	511	30
Australian Office of Finance Management	34	35	1
Australian Prudential Regulation Authority	561	572	11
Australian Securities and Investments Commission	1,571	1,534	-37
Australian Taxation Office	20,800	20,792	-8
Corporations and Market Advisory Committee	3	3	0
Inspector General of Taxation	6	6	0
National Competition Council	20	20	0
Productivity Commission	200	200	0
Total	**27,218**	**27,318**	**100**

(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 2005-06 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

The revenue and expense estimates and projections are based on a range of economic and other parameters. If the economic outlook was to differ from that presented in Statement 3, the revenue and expense estimates and projections would also change. Statement 3 discusses risks to the economic forecasts. Statement 2 discusses the sensitivity of revenue and expense estimates to changes in the 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.

Contingent liabilities

Contingent liabilities are 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.

Another class of contingent liability is uncalled capital, which reflects a financial commitment to an institution where no promissory note is issued by the Australian Government. Uncalled capital is primarily associated with international financial institutions such as the International Bank for Reconstruction and Development, the Asian Development Bank, the European Bank for Reconstruction and Development and the Multilateral Investment Guarantee Agency. When promissory notes are issued, such as in the case of the International Monetary Fund, the amounts are recorded in the general government balance sheet, so contingent liabilities (or assets) are not shown for those amounts.

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 2005. In general, information on contingent liabilities is based on information provided by Australian Government departments and agencies and is current to 31 March 2005 (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.

Table 1: Summary of changes to Statement of Risks since 2004-05 Budget and Mid-Year Economic and Fiscal Outlook

Specific risks — revenue	Status
Renegotiation of withholding tax rates in certain Australian double tax treaties	Modified
Fiscal risks — expenses	
Agriculture, Fisheries and Forestry	
Exceptional Circumstances assistance for drought affected farmers	Modified
Contingent liabilities — quantifiable	
Defence	
Guarantees	Modified
Employment and Workplace Relations	
Special Employee Entitlements Scheme for Ansett group employees	Deleted
Finance and Administration	
Australian Industry Development Corporation	Modified
ComLand Limited	Deleted
Foreign Affairs and Trade	
Export Finance and Insurance Corporation	Modified
Industry, Tourism and Resources	
Timor Sea Designated Authority — litigation	New
Transport and Regional Services	
Maritime industry reform	Modified
Treasury	
Guarantees under the *Commonwealth Bank Sale Act 1995*	Modified
Reserve Bank of Australia — guarantee	Modified
Uncalled capital subscriptions — international financial institutions	Modified
Various	
Asbestos related disease claims	Deleted
Contingent liabilities — unquantifiable	
Attorney-General's	
Southern Ocean surveillance	Modified
Communications, Information Technology and the Arts	
New South Wales Councils	Deleted
Defence	
Military Superannuation and Benefits Scheme — indemnity	New
Education, Science and Training	
Australian Nuclear Science and Technology Organisation — delays in the commissioning of Replacement Research Reactor	Deleted
Australian Nuclear Science and Technology Organisation — indemnity	New

Table 1: Summary of changes to Statement of Risks since 2004-05 Budget and Mid-Year Economic and Fiscal Outlook (continued)

Contingent liabilities — unquantifiable (continued)	
Finance and Administration	
Australian Technology Group — directors' indemnities	New
ComLand Limited — directors' indemnities	Modified
ComLand Limited — land remediation	Deleted
ComLand Limited — site contamination	New
Health Insurance Commission	Deleted
Members of Parliament Staff Employee Entitlements	Deleted
Potential claims relating to superannuation benefits	New
Sydney Airports Corporation Limited, Bankstown, Camden and Hoxton Park Airports — directors' indemnities	Modified
Tuggeranong Office Park Pty Ltd	Deleted
Tuggeranong Office Park Pty Ltd — shareholder indemnity	New
Indemnities relating to other former asset sales, privatisations and IT outsourcing projects	Modified
Health and Ageing	
CSL Limited	Modified
Industry, Tourism and Resources	
Litigation	New
Transport and Regional Services	
Deep vein thrombosis action	Modified
Tripartite deeds relating to the sale of Federal leased airports	Modified
Treasury	
Terrorism insurance — commercial cover	Modified

Note: Risks appearing in this Statement but not listed in the table above are substantially unchanged since disclosed in Budget Paper No. 1, *Budget Strategy and Outlook 2004-05*, Statement 11 or in *Mid-Year Economic and Fiscal Outlook 2004-05*, Appendix D.

FISCAL RISKS — REVENUE

The Government's revenue and policy measure forecasts, like all forecasts, are subject to a margin of error.

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. Over this period, the average error was 0.6 per cent, with the errors varying around this average by 2.7 percentage points. There are not enough data to assess the forecasting performance for accrual revenue.

However, in recent years revenue has grown more strongly than forecast. The revenue forecasting methodology has been adjusted from this Budget to align the revenue forecasts and projections more closely to recent experience (see Box 1, Statement 5).

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 general and specific risks influencing the accuracy of the revenue forecasts are outlined below.

General risks

The estimates and projections of revenue are subject to a number of general pressures that can affect taxation 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 taxation 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

The Australian Government is renegotiating its double tax treaties with several countries. Depending on the negotiated outcomes, changes to these treaties could have positive or 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. The forward estimates assume that there will be neither new drought declarations nor extensions of existing declarations. 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 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 is conditional on the Government being satisfied that arrangements are in place to deliver adequate telecommunications services, particularly in rural and regional Australia. The sale is also 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, so 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 Pharmaceutical Benefits Scheme usage patterns and/or doctors' charging patterns for Medicare Benefits Schedule services 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 of vaccinations. Potential costs cannot be precisely quantified at this stage.

Transport and Regional Services

Airservices Australia

On 31 August 2004, the Minister for Transport and Regional Services, pursuant to section 16 of the *Airservices Act 1995* (the Act), gave a direction to Airservices Australia (AA), which requires AA to provide an operating control tower and approach radar control services in certain volumes of airspace. Section 16(4) of the Act provides that AA may seek reimbursement from the Australian Government for any financial detriment it suffers as a result of complying with a direction. At this time, the quantum or nature of any financial detriment is uncertain, as is the nature of any consequent fiscal risk to the budget.

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

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 130 instances of contingencies that are unquantifiable, and 188 instances of quantifiable contingencies to the value of $4.8 billion. While these contingencies are considered remote, they have been reported in aggregate for completeness.

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 31 December 2004, AIDC's contingent liabilities, subject to Australian Government guarantee, were approximately $126 million in respect of guarantees and credit risk facilities.

In addition, AIDC had outstanding Australian Government guaranteed borrowings which totalled approximately $537 million as at the most current valuation of 31 December 2004. 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 AG, the international parent company that has taken over from UBS Warburg, manages this borrowing portfolio on behalf of AIDC. The UBS AG 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.

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 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 Sydney Airports Corporation Limited 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 the 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. The Australian Government's total contingent liability is $3.5 billion, comprising EFIC's liabilities to third parties ($2.9 billion) and EFIC's overseas investments insurance, contracts of insurance and guarantees ($546 million).

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.

Industry, Tourism and Resources

Timor Sea Designated Authority — litigation

PetroTimor, a subsidiary of the Portuguese registered company Oceanic Exploration, was granted a concession for petroleum exploration in an area of the Timor Sea by

Portugal in 1974. Following Indonesia's annexation of East Timor, PetroTimor ceased operations. With the subsequent Timor Gap Treaty between Australia and Indonesia (and now the Timor Sea Treaty between Australia and Timor-Leste), Oceanic Exploration is arguing that its rights have been alienated and it is currently seeking damages against the Timor Sea Designated Authority up to US$30 billion (the Australian Government share of which could be up to US$3 billion) through the United States Court for the District of Columbia.

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 are $107.1 million.

Treasury

Guarantees under the *Commonwealth Bank Sale Act*

Under the terms of the *Commonwealth Bank Sale Act 1995*, the Australian Government has guaranteed various superannuation and other liabilities amounting to around $12.8 billion. Of this amount, $9.3 billion was attributable to liabilities of the Commonwealth Bank of Australia at 30 September 2004 and $3.5 billion was attributable to liabilities of the Commonwealth Bank Officers' Superannuation Corporation at 30 June 2004.

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. Currently, notes on issue amount to $36.1 billion and the total guarantee is $43.8 billion.

International financial institutions — uncalled capital subscriptions

This contingent liability relates to the value of the uncalled portion of the Australian Government's shares 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$235.6 million), and the Multilateral Investment Guarantee Agency (US$26.5 million — estimated value A$34.3 million).

CONTINGENT LIABILITIES — UNQUANTIFIABLE

Attorney-General's

Native title agreements — access to geospatial data

The Australian Government has entered into agreements with state and territory government bodies and/or their agents to access their geospatial data. The data is essential to support the National Native Title Tribunal in achieving its outcome. Under these agreements, the Australian Government provides indemnities against third party claims arising from errors in the data.

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 has entered into contractual arrangements with P&O Maritime Services for the provision of maritime charter services until June 2006 to facilitate the Australian Customs Service and the Department of Agriculture, Fisheries and Forestry armed patrols of Australia's exclusive economic zone in the Southern Ocean.

The Australian Government will indemnify P&O Maritime Services against certain claims arising from the discharge of firearms or munitions, or where a steaming party is deployed to crew a seized vessel back to an Australian port. Whether those indemnity arrangements are maintained once the measure *Southern Ocean surveillance – continuation* is in place will depend on the outcome of contractual negotiations for the continued provision of maritime charter services.

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.

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 Limited for uninsured losses relating to specific heads of claims.

ASC Pty Ltd — 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 ASC Pty Ltd as it transitioned from being a producer of submarines to an agency for through-life support. EB/EBA staff commenced at ASC Pty Ltd 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 Pty Ltd 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 US$1 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 $145 million. There is identified potential for claims within the above 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.

Military Superannuation and Benefits Scheme — indemnity

The Military Superannuation and Benefits Scheme (MSBS) provides occupational superannuation benefits for members of the Australian Defence Force. Much of the day-to-day administration associated with the MSBS is conducted by ComSuper. Under the *Military Superannuation and Benefits Act 1991* the actions of ComSuper and its Commissioner are deemed to be those of the Military Superannuation and Benefits Board (MSB Board). Defence will indemnify the MSB Board for certain specified claims that are made in relation to acts of ComSuper and/or its Commissioner that are not recoverable elsewhere.

Education Science and Training

Australian Nuclear Science and Technology Organisation — indemnity

The Australian Government has indemnified the Australian Nuclear Science and Technology Organisation and its officers from liability that might be incurred from the conduct of activities authorised under the *Australian Nuclear Science and Technology Organisation Act 1987*. This indemnity is additional to the commercial insurance covers obtained from the Comcover Insurance Pool and other insurers.

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.

ASC Pty Ltd — 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 ASC Pty Ltd. This indemnity is ongoing.

ASC Pty Ltd — directors' indemnities

The Australian Government has indemnified the members of the board of ASC Pty Ltd for any claims and all legal costs arising from the result of the directors acting in accordance with the board's tasks and responsibilities as defined under the indemnity.

The Australian Government has indemnified the ASC Directors for any claim made against them as a result of complying with ASC's obligations under the Process Agreement between the Electric Boat Corporation (EBC), the Australian Government and ASC; and under the Services Agreement between ASC, the Australian Government, EBC and Electric Boat Australia.

Australian Technology Group — directors' indemnities

The Australian Government has indemnified Australian Government officials appointed as directors of the Australian Technology Group for liabilities relating to any action taken in their capacity as a director of the company. This includes any reasonable legal costs and expenses incurred by a director even after they have ceased to be a director.

ComLand Limited — directors' indemnities

Ongoing indemnities have been provided to former directors of ComLand Ltd, the former General Manager of ComLand Ltd and to DBYB Pty Ltd, against liabilities incurred in respect of assistance provided to the Australian Government during the ComLand scoping study and subsequent sale process.

ComLand Limited — site contamination

Footscray Land Limited is indemnified until 31 December 2019 in respect of certain contamination claims exceeding $7.5 million in aggregate at its Edgewater (Maribyrnong) site. St Marys Land Limited is indemnified until 31 December 2024 in respect of certain contamination claims and costs exceeding $25 million in aggregate at its St Marys (western Sydney) site.

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.

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 by the bank with the authority of the agency.

Potential claims relating to superannuation benefits

On 4 March 2005, the Supreme Court of the Australian Capital Territory found against the Commonwealth of Australia on a claim for negligence and breach of contract relating to superannuation benefits for a former employee of the Department of the Interior. This is considered to be a test case for several hundred named potential plaintiffs. In addition there is potential for more claims to arise from other former employees. An appeal against the decision of the ACT Supreme Court was lodged in March 2005.

Sydney Airports Corporation Limited, Bankstown, Camden and Hoxton Park Airports — 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, and Hoxton Park 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 — shareholder indemnity

As part of the arrangements for Tuggeranong Office Park, the Australian Government can acquire the shares of the Tuggeranong Office Park Pty Ltd for $100 subject to certain conditions. In its capacity as purchaser of the shares, the Australian Government has indemnified each Shareholder for all 'losses, liabilities, costs, expenses and damages' incurred by virtue of their shareholding. If a capital gains tax liability were to accrue to the Shareholders, the Australian Government may be required to reimburse the Shareholders. The Department of Finance and Administration will be seeking advice from the Australian Tax Office on this issue.

Indemnities relating to other former asset sales, privatisations and IT outsourcing projects

Ongoing indemnities have been given in respect of a range of asset sales, privatisations and IT outsourcing projects that have been conducted by the Department of Finance and Administration (Finance), and the former Office of Asset Sales and Commercial Support and its predecessors. The probability of an action being made under one of these indemnities diminishes over time. Details of indemnities in respect of the other asset sales and privatisations have been provided in previous Budget and Mid-Year Economic and Fiscal Outlook papers, and previous annual reports for Finance and the Office of Asset Sales and Commercial Support.

Indemnities (including the year they were raised) are still current for: ADI Ltd (1998), Australian Airlines (1991), Australian Industry Development Corporation (1996), Australian Multimedia Enterprise (1997), Australian National Rail Commission and National Rail Corporation Ltd (1997 and 2000), Commonwealth Accommodation and Catering Services (1988), Commonwealth Bank of Australia (1993 to 1996), Commonwealth Funds Management and Total Risk Management (1996 to 1997), Essendon Airport Ltd (2001), Federal Airports Corporation's Airports (1995 to 1997), Home Loans Insurance Commission Ltd (1996), Health Insurance Commission (2000), National Transmission Network (1999), Telstra (1996 and 1999), Wool International (1999). The Department does not currently expect any action to be taken in respect of these indemnities.

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, the ARCBS and the states and territories. The NMF is covered by a Memorandum of Understanding (MoU) between the Australian Government, states and territories, and the ARCBS. This will be amended to incorporate the operations of the Jurisdictional Blood Committee (JBC) and the National Blood Authority. The MoU 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 JBC considers a report provided by the National Funds Manager to determine the level of funds required. Each party must contribute funds, as determined by JBC, 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.

CSL Limited

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 occurred during the operation of the Plasma Fractionation Agreement, from 1 January 1994 to 31 December 2004. Where alternative cover was not arranged by CSL Limited, the Australian Government may have a contingent liability. Given the open-ended nature of some of the indemnities, damages and risk cannot be quantified. No similar indemnities have been given to CSL Limited in the new Plasma Products Agreement operating from 1 January 2005.

Medical Indemnity 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, currently $20 million. 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 medical indemnity insurer, 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. 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 (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.

Claim of unlawful detention on Nauru

On 16 December 2003, 325 plaintiffs claiming to be detained on Nauru commenced an action in the Supreme Court of Victoria. The claim alleges that the plaintiffs have been detained at the request of, or by agents of, the Australian Government, and that the detention amounts to false imprisonment. The plaintiffs seek a declaration that they have been falsely imprisoned by the Australian Government, an injunction to restrain the Australian Government or its agents from continuing to detain the plaintiffs, and damages. The case has not yet been listed for hearing.

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.

Litigation

The Department of Industry, Tourism and Resources is involved in litigation concerning the Textile, Clothing and Footwear (TCF) Strategic Investment Programme (SIP). The TCF SIP is an entitlement-based programme that provides grants to support eligible capital investment and product innovation by TCF firms. The litigation relates to disputed claims of eligibility under the TCF SIP. There are potential risks associated with flow-on claims and the risk cannot yet be accurately quantified.

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 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. There have been 484 writs issued against CASA, spanning 1995 to 2002. The Australian Government's exposure is limited to claims for the years 1995 to 5 July 1998, as CASA was covered by a Commonwealth Deed of Indemnity in relation to the performance of its regulatory functions. Ninety-nine writs have been issued against CASA which are covered by the Deed of Indemnity. The remaining writs are covered by CASA's commercial insurance.

A test case (*Povey v Qantas and British Airways and CASA*) is currently before the High Court on appeal from the Victorian Supreme Court. However, until the High Court proceedings have been finalised, it is not possible to determine what (if any) liability CASA may have in relation to deep vein thrombosis.

Maritime Industry Finance Company Limited — board members' indemnity

Indemnities for Maritime Industry Finance Company Limited board members have been provided to protect them against civil claims relating to their employment and conduct as directors.

Tripartite deeds relating to the sale of Federal leased airports

Tripartite deeds apply to 12 Federal leased airports (Adelaide, Alice Springs, Bankstown, Brisbane, Canberra, Coolangatta, Darwin, Launceston, Melbourne, Perth, Sydney and Townsville). 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.

Terrorism insurance — commercial cover

The *Terrorism Insurance Act 2003* (the Act) established a scheme for replacement terrorism insurance covering damage to commercial property including associated business interruption and public liability. The scheme plans to accumulate approximately $300 million from reinsurance premiums paid to the Australian Reinsurance Pool Corporation (ARPC) to help meet administrative expenses and future claims. The Commonwealth guarantees to pay any liabilities of the ARPC, but the Treasurer must declare a reduced payout rate to insureds if the Commonwealth's liability would otherwise exceed $10 billion.

PART 5
PUBLIC SECTOR TRENDS

This part addresses recent 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 Government and state/local levels of government, and also at the consolidated level. These measures are discussed in greater detail in Statement 8.

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 statement, 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.

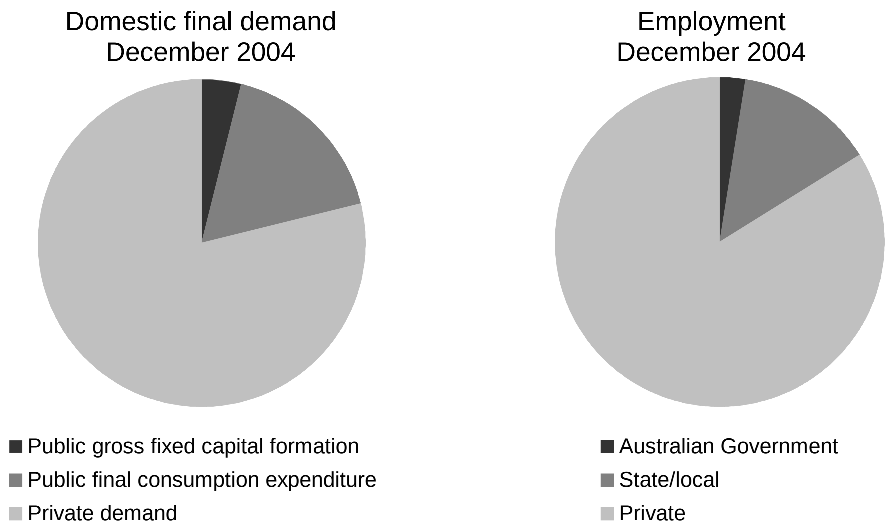
STATEMENT 12: TRENDS IN PUBLIC SECTOR FINANCES

SIZE AND STRUCTURE OF THE PUBLIC SECTOR

The size and structure of Australia's public sector provides a useful context for interpreting trends in the total public sector. The total public sector[1] constitutes a significant portion of the Australian economy (over 20 per cent of domestic final demand).

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 38 per cent of public final demand, while the state/local level of government accounts for 62 per cent.

Chart 1: Contribution of public and private sectors



Sources: ABS Cat. Nos. 6248.0, 6202.0 and 5206.0.

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1 The total public sector includes the total non-financial public sector (comprised of the general government sector and the public non-financial corporations sector) and the public financial corporations sector for the Australian Government and state/local levels of government.

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. Transfer payments, such as Australian Government income support payments, are not included in the Australian Government public final demand. Rather, these payments, and 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 14 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. The state/local sector's larger share reflects that 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 total non-financial public sector (NFPS) and the total public financial corporations sector. The total 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 revenue 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 be a surplus of 0.8 per cent of Gross Domestic Product (GDP) in 2004-05. The surplus is expected to be maintained at 0.8 per cent of GDP until 2008-09, when the surplus is expected to rise to 0.9 per cent of GDP.

The fiscal balance of the state/local general government sector is expected to be a deficit of 0.1 per cent of GDP in 2004-05. The deficit is projected to increase to 0.3 per cent of GDP in 2005-06. This projection is predominantly based on state 2004-05 mid-year reviews, since only Victoria, the Australian Capital Territory and the Northern Territory have released their 2005-06 Budgets.

The consolidated[2] PNFC fiscal balance is expected to be in deficit in 2004-05 by 0.5 per cent of GDP. This includes an estimated Australian Government PNFC fiscal surplus of 0.2 per cent of GDP. The decrease in consolidated PNFC revenue 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.

2 When combined, the Australian Government, state/local governments and universities are referred to as the 'consolidated public sector'.

Table 1: General government fiscal balance by level of government (per cent of GDP)[(a)]

	Australian Government			State/local			Consolidated		
	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance
1996-97	26.8	27.6	-0.8	na	na	na	na	na	na
1997-98	26.3	26.6	-0.4	na	na	na	na	na	na
1998-99	25.8	24.9	0.7	17.6	16.8	0.3	38.2	36.4	1.0
1999-00	26.8	25.1	1.9	17.4	16.5	0.4	39.0	36.3	2.3
2000-01	24.2	23.5	0.8	17.2	16.7	-0.1	38.5	37.3	0.7
2001-02	22.8	23.3	-0.5	17.1	16.5	0.0	36.8	36.7	-0.4
2002-03	23.1	22.5	0.6	17.1	16.4	0.3	37.8	36.4	1.0
2003-04	23.1	22.4	0.6	17.3	16.3	0.5	38.1	36.3	1.3
2004-05(e)	23.5	22.6	0.8	16.8	16.3	-0.1	37.7	36.1	0.9
2005-06(e)	**23.1**	**22.2**	**0.8**	**16.2**	**15.7**	**-0.3**	**36.7**	**35.2**	**0.7**
2006-07(p)	23.0	22.2	0.8	na	na	na	na	na	na
2007-08(p)	23.2	22.4	0.8	na	na	na	na	na	na
2008-09(p)	23.1	22.3	0.9	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.
(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)]

	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	6.3	-0.5	10.9	10.7	-0.6
1999-00	4.1	3.7	0.2	5.9	5.6	0.3	9.9	9.4	0.5
2000-01	3.8	3.7	-0.1	5.6	5.4	0.2	9.5	9.0	0.1
2001-02	3.7	3.5	0.1	4.9	4.7	-0.2	8.6	8.2	-0.1
2002-03	3.2	3.0	0.3	4.6	4.6	-0.4	7.8	7.6	-0.1
2003-04	3.1	2.9	0.3	4.6	4.5	-0.3	7.8	7.3	0.0
2004-05(e)	3.1	2.9	0.2	4.4	4.4	-0.7	7.5	7.3	-0.5
2005-06(e)	**3.0**	**2.9**	**0.0**	**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.
(e) Estimates.
na Data not available.

Table 3: Total non-financial public sector fiscal balance by level of government (per cent of GDP)[(a)]

	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	29.8	28.6	0.5	21.4	20.6	-0.1	46.0	43.9	0.4
1999-00	30.2	27.8	2.3	21.2	20.1	0.7	46.3	42.7	3.0
2000-01	27.4	26.6	0.7	21.0	20.3	0.0	45.4	43.9	0.7
2001-02	25.9	26.2	-0.4	20.1	19.4	-0.2	43.0	42.5	-0.5
2002-03	25.6	24.9	0.9	20.0	19.2	-0.1	43.3	41.6	0.9
2003-04	25.5	24.5	0.9	20.1	18.9	0.2	43.4	41.1	1.2
2004-05(e)	26.0	24.9	1.0	19.5	18.9	-0.8	42.9	41.1	0.3
2005-06(e)	**25.5**	**24.5**	**0.8**	**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.
(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 of Chart 2 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 also 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 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 2004-05, compared to 0.8 per cent of GDP in 2003-04. 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 maintained a cash surplus position through much of the 1990s. The sector is projected to be in deficit in 2004-05, due to deficits in the PNFC sector of nearly all states.

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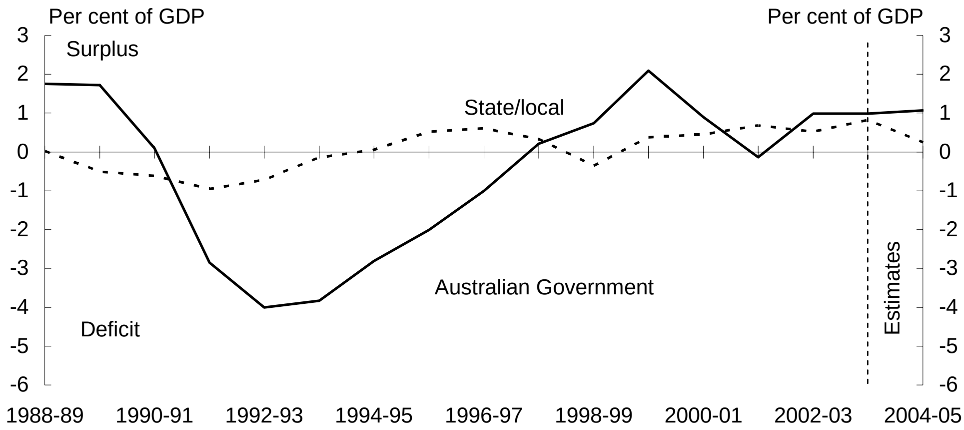
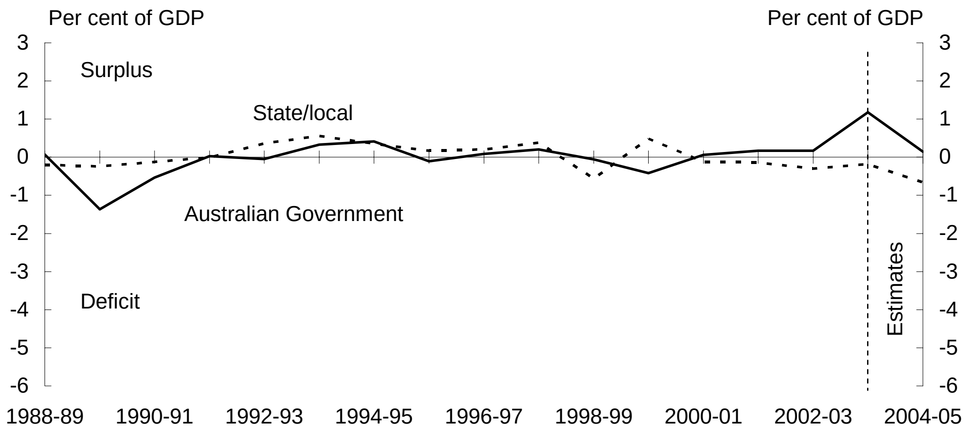
3 For example, see NSW's *2004-05 Half-Yearly Budget Review*, pp.10, 17.

Chart 2: Cash surplus by sector and level of government

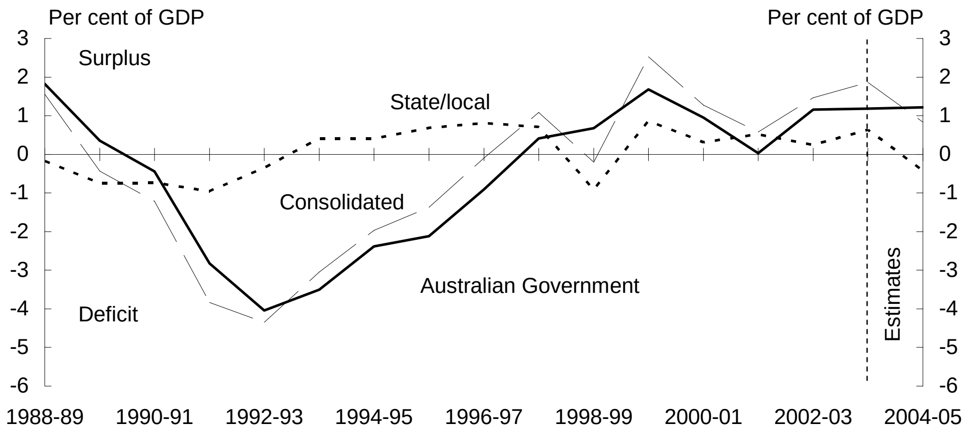
A: General government



B: Public non-financial corporations



C: Non-financial public sector

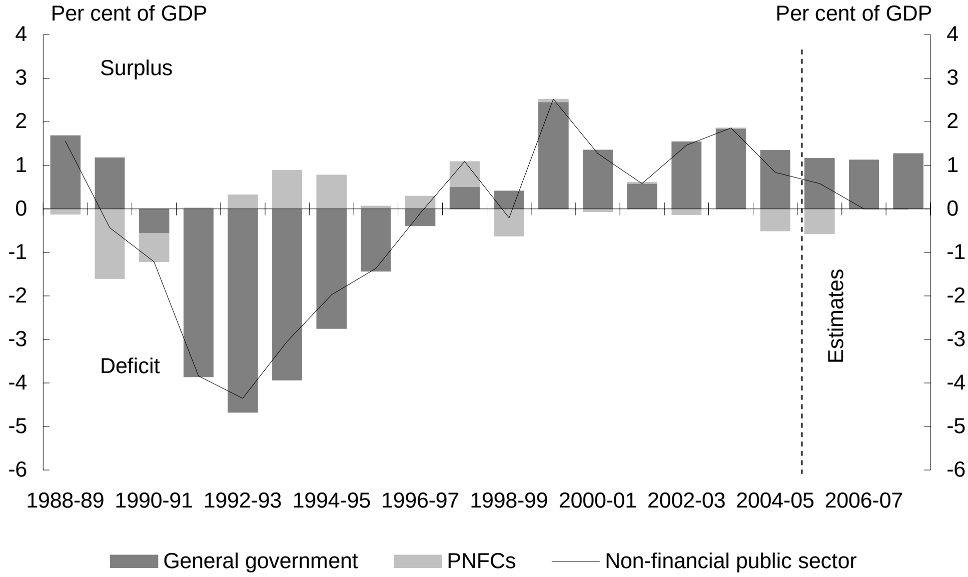


Non-financial public sector

It is estimated that the consolidated NFPS will achieve a cash surplus of 0.8 per cent of GDP in 2004-05.

Chart 3 illustrates that the consolidated NFPS was generally in a deficit position during the early to mid 1990s. The deficit peaked at 4.4 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 2004-05, while general government data are available to 2007-08.

Receipts and payments

Chart 4 shows trends in general government cash receipts and payments at the Australian Government, 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 38.9 per cent of GDP in 1999-2000 to 38.0 per cent of GDP in 2004-05, due to the Australian Government's tax reforms, which included significant personal income tax cuts and the abolition at the state level of financial institutions duty and stamp duty on quoted marketable securities.

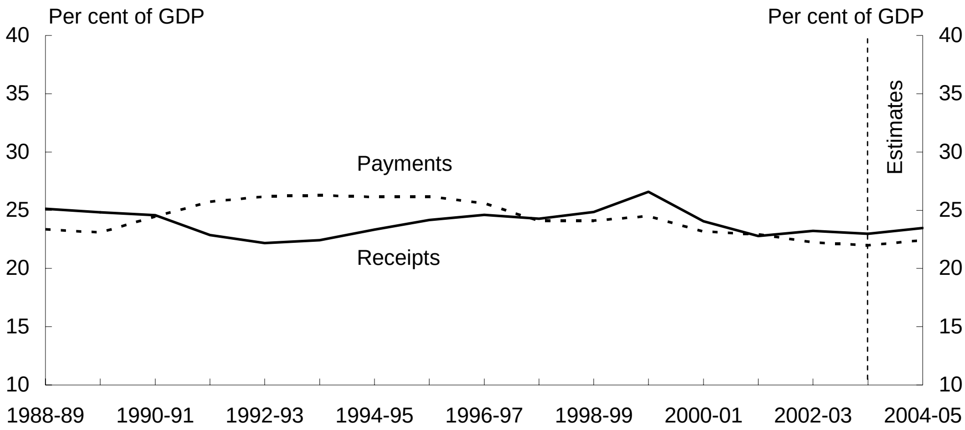
The improvement in state finances from 1991-92 is shown in Panel B of Chart 4. The state/local cash deficit peaked at 1 per cent of GDP in 1991-92. After 1991-92, deficits continued to be reduced until the state/local sector achieved a surplus in 1994-95. Since then, the state/local cash position has 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 and GST. In 2004-05, the sector is expected to record a surplus of 0.2 per cent of GDP.

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 B and A of Chart 4 respectively, 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.

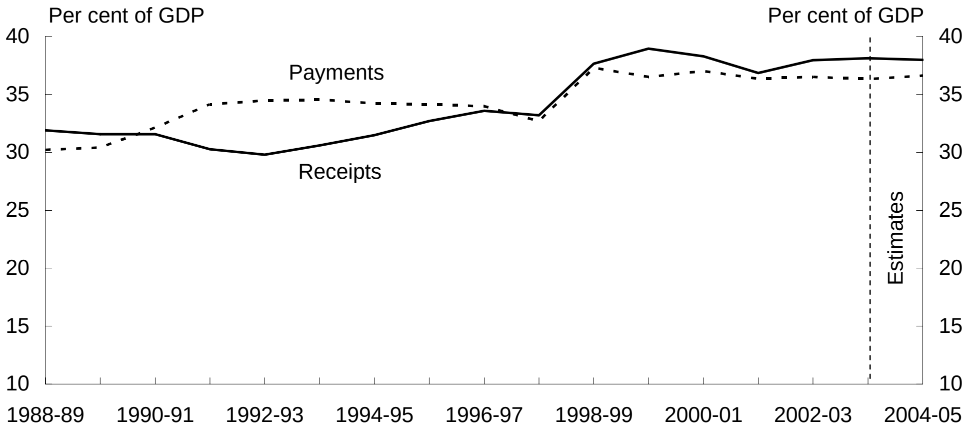
PNFC privatisations during the 1990s have occurred in two main sectors — electricity and gas (such as Victorian and South Australian electricity assets) and transport and communications (such as the partial sale of Telstra). Proceeds of asset sales have largely been used to reduce, or contain, the growth 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

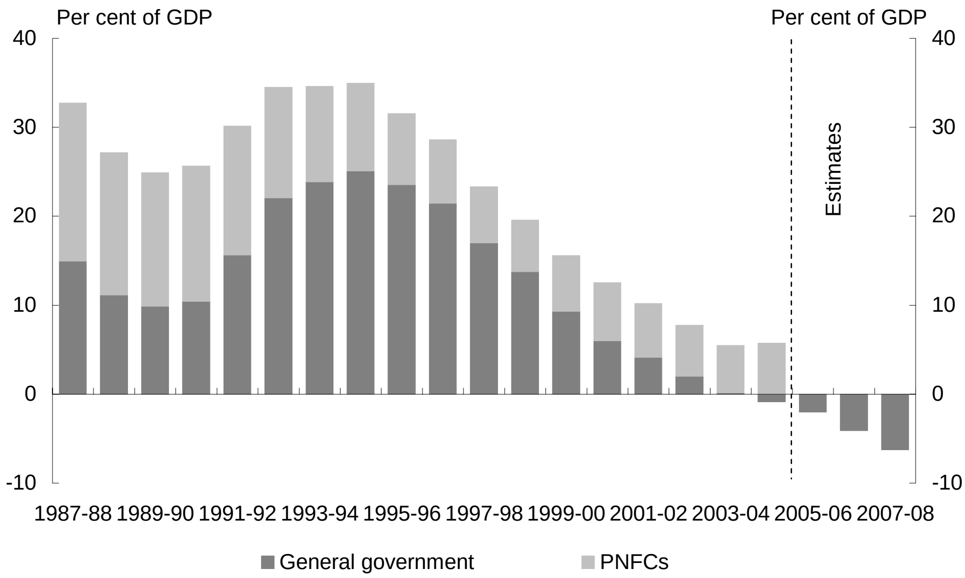
Chart 5 shows that consolidated general government net debt as a share of GDP is expected to continue to decline over the forward years. Consolidated NFPS net debt is estimated to be 4.9 per cent of GDP in 2004-05, compared with the most recent peak of 35 per cent in 1994-95.

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 sectors are only available to 2004-05, while data for the general government sector are available to 2007-08.

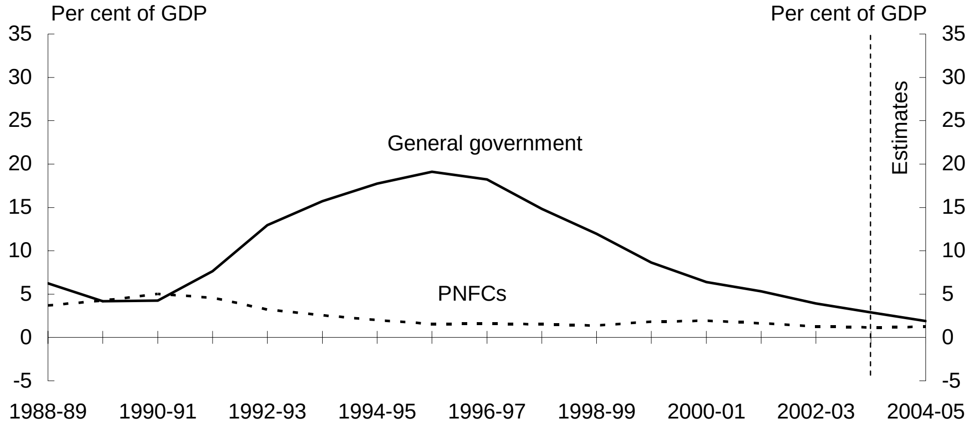
Panel A of Chart 6 shows that most Australian Government net debt is held by the general government sector whereas Panel B of Chart 6 shows that, since 2002-03, all state/local net debt is held in the PNFC sector.

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. Since then, successive surpluses and asset sales (most notably the partial sale of Telstra) have reduced Australian Government general government sector net debt to an expected 1.9 per cent of GDP in 2004-05.

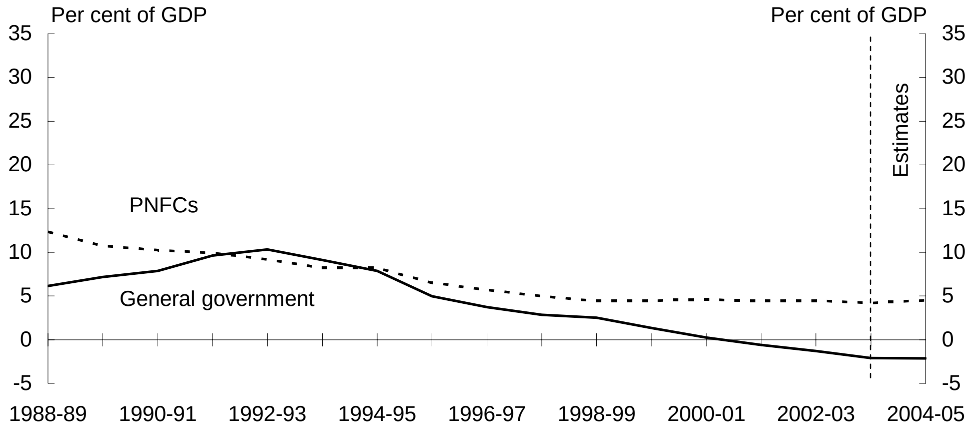
In contrast, state/local general government net debt grew more modestly in the early 1990s and is expected to decline from a peak of 10.3 per cent of GDP in 1992-93 to a net debt position of approximately -2.1 per cent of GDP in 2004-05, as shown in Panel B of Chart 6. This improvement within the state/local 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 2005-06*).

Chart 6: Non-financial public sector net debt by level of government and sector (as at end of financial year)

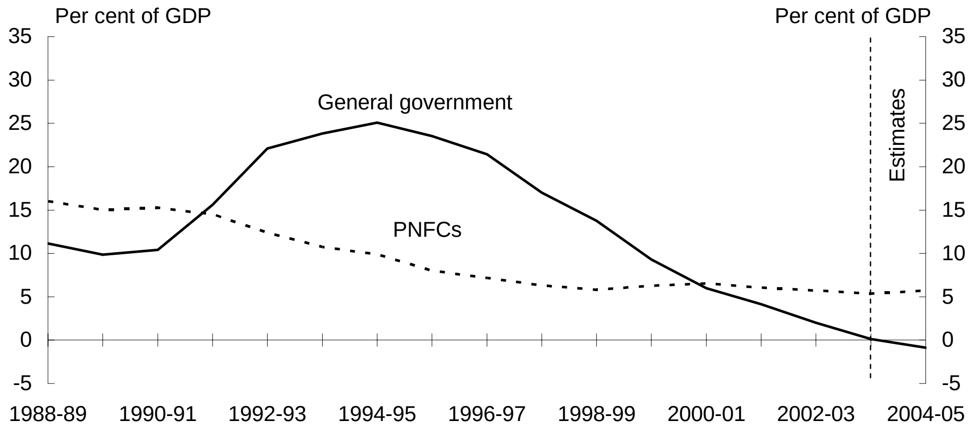
A: Australian Government



B: State/local



C: Consolidated



NET WORTH

The state/local general government sector has an estimated positive net worth of 60 per cent of GDP in 2005-06. 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, has declined as a 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 balance sheets of the state and local governments.

Table 4: General government net worth by level of government (as at end of financial year)

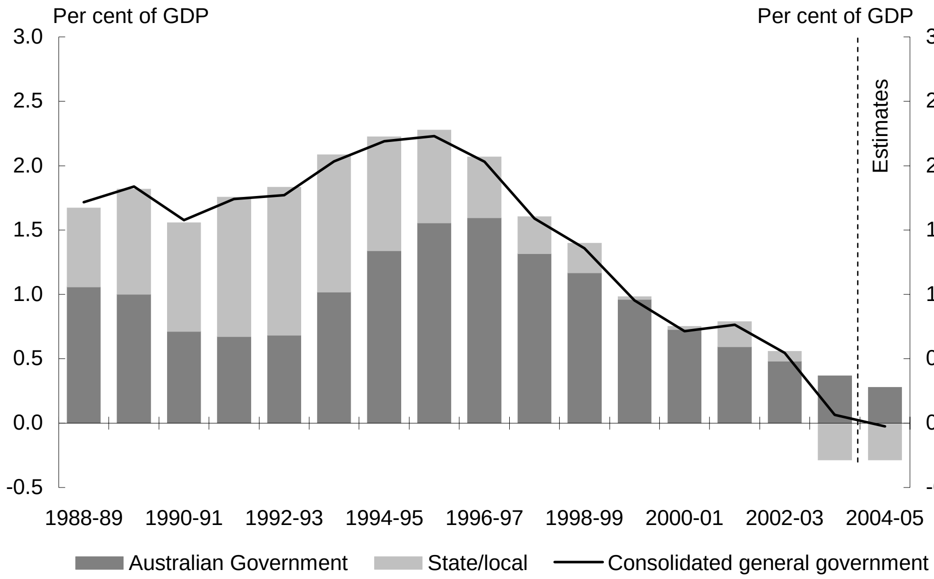
	Australian Government(a)		State/local		Consolidated	
	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP
1996-97	-74,354	-14.1	na	na	na	na
1997-98	-68,544	-12.3	na	na	na	na
1998-99	-76,150	-12.9	362,395	61.5	304,309	51.6
1999-00	-40,552	-6.5	390,336	62.6	368,850	59.2
2000-01	-43,299	-6.5	404,931	60.6	381,557	57.1
2001-02	-48,429	-6.8	426,234	59.8	399,470	56.0
2002-03	-53,251	-7.0	471,065	62.1	441,125	58.2
2003-04	-39,544	-4.9	515,014	63.3	500,703	61.5
2004-05(e)	-34,126	-4.0	538,684	62.4	531,568	61.6
2005-06(e)	**-27,779**	**-3.0**	**556,854**	**60.0**	**558,226**	**60.2**
2006-07(p)	-20,421	-2.1	na	na	na	na
2007-08(p)	-13,708	-1.4	na	na	na	na
2008-09(p)	-5,922	-0.6	na	na	na	na

(a) 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 Government Finance Statistics (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 reduce to around 0 per cent of GDP in 2004-05 due to reduced Australian and state/local general government net debt since 1995-96 and lower interest rates in recent years.

Chart 7: General government net interest payments



The contribution of the PNFC sector to NFPS net interest payments has decreased significantly since 1997-98 as reduced investment by PNFCs, improved performance by PNFCs and privatisations have reduced PNFC net debt as a share of GDP.

APPENDIX A: SUPPLEMENTARY CASH TABLES

Table A1: Consolidated cash receipts, payments and cash surplus by institutional sector as a per cent of GDP

	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	34.5	-4.7	3.6	5.0	0.3	32.0	38.1	-4.4
1993-94	30.6	34.5	-3.9	3.8	4.4	0.9	32.8	37.3	-3.0
1994-95	31.5	34.2	-2.7	3.5	4.5	0.8	33.4	37.3	-2.0
1995-96	32.7	34.1	-1.4	3.0	4.6	0.1	34.0	37.0	-1.4
1996-97	33.6	34.0	-0.4	3.1	4.2	0.3	34.5	36.1	-0.1
1997-98	33.2	32.7	0.5	3.0	3.7	0.6	34.6	34.8	1.1
1998-99	37.7	37.3	0.4	na	na	-0.6	na	na	-0.2
1999-00	38.9	36.5	2.5	na	na	0.1	na	na	2.5
2000-01	38.3	37.0	1.4	na	na	-0.1	na	na	1.3
2001-02	36.9	36.3	0.6	na	na	0.0	na	na	0.6
2002-03	38.0	36.5	1.5	na	na	-0.1	na	na	1.5
2003-04	38.1	36.3	1.8	na	na	0.0	na	na	1.9
2004-05(e)	38.0	36.6	1.3	na	na	-0.5	na	na	0.8
2005-06(e)	**37.1**	**35.9**	**1.2**	**na**	**na**	**na**	**na**	**na**	**na**
2006-07(p)	36.8	35.7	1.1	na	na	na	na	na	na
2007-08(p)	37.0	35.7	1.3	na	na	na	na	na	na

(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

	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	-4.4
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	-0.9	-0.2
1999-00	1.7	0.9	2.5
2000-01	1.0	0.3	1.3
2001-02	0.0	0.5	0.6
2002-03	1.2	0.2	1.5
2003-04	1.2	0.6	1.9
2004-05(e)	1.2	-0.4	0.8
2005-06(e)	**1.1**	**na**	**na**

(e) Estimates.
na Data not available.

Table A3: General government net interest payments by level of government

	Australian Government(a)		State/local	
	$m	Per cent of GDP	$m	Per cent of GDP
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	1,376	0.2
1999-00	6,014	1.0	146	0.0
2000-01	4,855	0.7	165	0.0
2001-02	4,238	0.6	1,399	0.2
2002-03	3,641	0.5	597	0.1
2003-04	2,994	0.4	-2,339	-0.3
2004-05(e)	2,396	0.3	-2,482	-0.3
2005-06(e)	**2,759**	**0.3**	**na**	**na**
2006-07(p)	1,159	0.1	na	na
2007-08(p)	-249	0.0	na	na
2008-09(p)	-1,339	-0.1	na	na

(a) 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 GFS standards.
(e) Estimates.
(p) Projections.
na Data not available.

Table A4: Non-financial public sector net debt[(a)]

	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	11.2	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	10.8	154,460	34.6
1994-95	83,492	17.8	37,039	7.9	117,973	25.1	46,482	9.9	164,455	35.0
1995-96	95,831	19.1	24,981	5.0	118,053	23.6	40,135	8.0	158,188	31.6
1996-97	96,281	18.2	19,757	3.7	113,236	21.4	37,748	7.1	150,984	28.6
1997-98	82,935	14.8	15,937	2.9	95,122	17.0	35,371	6.3	130,493	23.3
1998-99	70,402	11.9	14,783	2.5	81,203	13.8	34,233	5.8	115,436	19.6
1999-00	53,768	8.6	8,306	1.3	58,068	9.3	39,135	6.3	97,203	15.6
2000-01	42,651	6.4	1,530	0.2	39,974	6.0	43,757	6.5	83,732	12.5
2001-02	38,024	5.3	-4,309	-0.6	29,517	4.1	43,262	6.1	72,779	10.2
2002-03	29,665	3.9	-9,895	-1.3	15,308	2.0	43,514	5.7	59,362	7.8
2003-04	23,421	2.9	-17,229	-2.1	967	0.1	43,640	5.4	45,059	5.5
2004-05(e)	16,328	1.9	-18,356	-2.1	-7,568	-0.9	49,441	5.7	41,873	4.9
2005-06(e)	**6,080**	**0.7**	**-18,802**	**-2.0**	**-18,601**	**-2.0**	**na**	**na**	**na**	**na**
2006-07(p)	-14,031	-1.5	-19,438	-2.0	-39,701	-4.1	na	na	na	na
2007-08(p)	-34,649	-3.4	-21,953	-2.2	-63,203	-6.3	na	na	na	na
2008-09(p)	-56,389	-5.3	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.

(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) Government Finance Statistics (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 Government, 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 2003-04 Government Finance Statistics (Cat. No. 5512.0), Australian Government Final Budget Outcomes and jurisdictions' 2004-05 mid-year reports and, for Victoria, the Australian Capital Territory and the Northern Territory only, 2005-06 Budgets. As indicated in Budget Paper No. 1, Budget Strategy and Outlook 2004-05, Statement 12, a review of the accrual time series data by the ABS, in consultation with all Treasuries, has been occurring. The review is resulting in improved quality in the time series data and has resulted in some changes to the series. Further revisions are expected over the next year.

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), *2003-04 Government Finance Statistics* (ABS Cat. No. 5512.0) and

Statement 13. Net debt numbers from 2004-05 are taken from jurisdictions' 2004-05 mid-year reports, 2005-06 budgets and Australian Government Treasury estimates.

Australian Government budget aggregates, including net debt for 1999-2000 onwards, have been revised relative to the *Mid-Year Economic and Fiscal Outlook 2002-03* 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.

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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 back-casting 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 sector 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.

Occasionally classification changes are made that require revisions to the historic series. Where appropriate, the changes are back-cast to 1999-2000 to ensure that data is consistent across the accrual period. For example, the back-casting to account for the market valuation of net debt as discussed on page 2-12 of the Budget Paper No. 1, *Budget Strategy and Outlook 2003-04*.

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 underlying cash balance(a)

	Receipts			Payments			Future Fund earnings	Underlying cash balance(b)	
	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP	$m	$m	Per cent of GDP
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	24.4	-	-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	5.1	26.9	75,392	0.6	27.7	-	-2,247	-0.8
1987-88	81,217	3.3	26.1	79,440	-2.0	25.6	-	1,777	0.6
1988-89	88,369	0.3	25.1	82,202	-4.6	23.4	-	6,167	1.8
1989-90	95,517	1.7	24.8	88,882	1.7	23.1	-	6,635	1.7
1990-91	97,705	-2.5	24.6	97,333	4.4	24.5	-	372	0.1
1991-92	92,966	-6.9	22.9	104,551	5.1	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	5.2	22.4	117,252	4.3	26.3	-	-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	7.7	24.2	131,182	4.2	26.2	-	-10,077	-2.0
1996-97	129,845	5.2	24.6	135,126	1.0	25.6	-	-5,281	-1.0
1997-98	135,779	3.1	24.3	134,608	-1.8	24.1	-	1,171	0.2
1998-99	146,496	7.4	24.8	142,159	5.2	24.1	-	4,337	0.7
1999-00	165,806	na	26.6	152,747	na	24.5	-	13,059	2.1
2000-01	160,829	-7.2	24.1	154,858	-3.0	23.2	-	5,970	0.9
2001-02	162,524	-1.2	22.8	163,507	3.3	22.9	-	-983	-0.1
2002-03	176,147	5.0	23.2	168,661	0.0	22.2	-	7,486	1.0
2003-04	186,971	2.4	23.0	178,935	2.4	22.0	-	8,036	1.0
2004-05(e)	202,662	4.3	23.5	193,441	4.1	22.4	-	9,221	1.1
2005-06(e)	**214,515**	**1.3**	**23.1**	**205,132**	**1.5**	**22.1**	**462**	**8,921**	**1.0**
2006-07(p)	221,891	2.7	22.9	213,015	3.1	22.0	943	7,933	0.8
2007-08(p)	232,525	4.1	23.1	223,029	4.0	22.1	997	8,500	0.8
2008-09(p)	244,245	3.1	23.0	233,907	2.9	22.1	1,054	9,284	0.9

(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.

(b) Underlying cash balance is equal to receipts less payments less expected Future Fund earnings. For the purposes of consistent comparison with years prior to 2005-06 , Future Fund earnings should be added back to the underlying cash balance.

(e) Estimates.

(p) Projections.

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
1971-72	7,887	3.3	18.6	940	3.3	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	2.3	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	5.3	24.4	6,678	3.7	2.5	73,145	5.1	26.9
1987-88	75,076	5.1	24.2	6,141	-14.5	2.0	81,217	3.3	26.1
1988-89	83,452	2.4	23.7	4,917	-26.2	1.4	88,369	0.3	25.1
1989-90	90,773	2.3	23.6	4,744	-9.2	1.2	95,517	1.7	24.8
1990-91	92,739	-2.6	23.3	4,966	-0.2	1.2	97,705	-2.5	24.6
1991-92	87,364	-7.9	21.5	5,602	10.3	1.4	92,966	-6.9	22.9
1992-93	88,760	0.6	20.8	5,688	0.5	1.3	94,448	0.5	22.2
1993-94	93,362	4.3	20.9	6,780	18.2	1.5	100,142	5.2	22.4
1994-95	104,921	11.5	22.3	4,799	-29.7	1.0	109,720	8.7	23.3
1995-96	115,700	7.6	23.1	5,405	9.9	1.1	121,105	7.7	24.2
1996-97	124,559	5.6	23.6	5,286	-4.1	1.0	129,845	5.2	24.6
1997-98	130,984	3.7	23.4	4,795	-10.6	0.9	135,779	3.1	24.3
1998-99	141,105	7.3	23.9	5,391	11.9	0.9	146,496	7.4	24.8
1999-00	150,695	na	24.2	15,111	na	2.4	165,806	na	26.6
2000-01	146,056	-7.2	21.9	14,774	-6.4	2.2	160,829	-7.2	24.1
2001-02	147,544	-1.2	20.7	14,980	-0.8	2.1	162,524	-1.2	22.8
2002-03	160,661	5.5	21.2	15,487	0.2	2.0	176,147	5.0	23.2
2003-04	172,243	3.4	21.2	14,729	-8.2	1.8	186,971	2.4	23.0
2004-05(e)	186,205	4.1	21.6	16,457	7.6	1.9	202,662	4.3	23.5
2005-06(e)	**197,829**	**1.6**	**21.3**	**16,686**	**-3.0**	**1.8**	**214,515**	**1.3**	**23.1**
2006-07(p)	204,975	2.9	21.2	16,917	0.7	1.7	221,891	2.7	22.9
2007-08(p)	214,781	4.1	21.3	17,744	4.2	1.8	232,525	4.1	23.1
2008-09(p)	225,895	3.2	21.3	18,350	1.5	1.7	244,245	3.1	23.0

(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.

(e) Estimates.

(p) Projections.

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		Net interest payments(b)	
	$m	Per cent of GDP	$m	Per cent of GDP
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	17.8	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	23,421	2.9	2,994	0.4
2004-05(e)	16,328	1.9	2,396	0.3
2005-06(e)	**6,080**	**0.7**	**2,759**	**0.3**
2006-07(p)	-14,031	-1.5	1,159	0.1
2007-08(p)	-34,649	-3.4	-249	0.0
2008-09(p)	-56,389	-5.3	-1,339	-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) Excludes superannuation related interest flows.
(e) Estimates.
(p) Projections.

Table 4: Australian Government general government sector revenue, expenses, net capital investment, fiscal balance and net worth[(a)]

	Revenue		Expenses(d)		Net capital investment		Fiscal balance(d)		Net worth(b)(c)(d)	
	$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
1997-98	146,820	26.3	148,646	26.6	147	0.0	-1,973	-0.4	-68,544	-12.3
1998-99	151,897	25.8	146,620	24.9	1,433	0.2	3,844	0.7	-76,150	-12.9
1999-00	166,875	26.8	156,209	25.1	-1,225	-0.2	11,892	1.9	-40,552	-6.5
2000-01	161,789	24.2	157,382	23.5	-1,168	-0.2	5,575	0.8	-43,299	-6.5
2001-02	162,599	22.8	166,401	23.3	-369	-0.1	-3,433	-0.5	-48,429	-6.8
2002-03	175,191	23.1	170,676	22.5	-219	0.0	4,734	0.6	-53,251	-7.0
2003-04	187,559	23.1	182,005	22.4	724	0.1	4,830	0.6	-39,544	-4.9
2004-05(e)	202,666	23.5	195,012	22.6	652	0.1	7,003	0.8	-34,126	-4.0
2005-06(e)	**214,511**	**23.1**	**206,081**	**22.2**	**1,020**	**0.1**	**7,410**	**0.8**	**-27,779**	**-3.0**
2006-07(p)	222,882	23.0	214,806	22.2	617	0.1	7,458	0.8	-20,421	-2.1
2007-08(p)	233,405	23.2	225,400	22.4	1	0.0	8,003	0.8	-13,708	-1.4
2008-09(p)	245,326	23.1	236,568	22.3	-264	0.0	9,022	0.9	-5,922	-0.6

(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 *Final Budget Outcome 2002-03*, a reliable actuarial measure was not available. Following an actuarial review a provision for asbestos related claims was included in the audited *Consolidated Financial Statements 2002-03*.
(d) The increases in expenses and decreases in fiscal balance and net worth arise from a change in recognition of family tax benefits and other expenses from a cash to an accrual basis.
(e) Estimates.
(p) Projections.

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
2000-01	151,437	na	22.7	10,352	na	1.5	161,789	na	24.2
2001-02	150,077	-3.1	21.0	12,522	18.3	1.8	162,599	-1.7	22.8
2002-03	163,232	5.4	21.5	11,958	-7.4	1.6	175,191	4.4	23.1
2003-04	175,058	3.5	21.5	12,501	0.9	1.5	187,559	3.3	23.1
2004-05(e)	190,201	4.6	22.0	12,465	-4.0	1.4	202,666	4.0	23.5
2005-06(e)	**201,267**	**1.2**	**21.7**	**13,245**	**1.7**	**1.4**	**214,511**	**1.3**	**23.1**
2006-07(p)	208,999	3.1	21.6	13,883	4.1	1.4	222,882	3.2	23.0
2007-08(p)	218,798	4.0	21.7	14,607	4.5	1.4	233,405	4.0	23.2
2008-09(p)	230,120	3.2	21.7	15,206	2.1	1.4	245,326	3.1	23.1

(e) Estimates.
(p) Projections.
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	Underlying cash balance(b)	Receipts	Payments	Cash surplus	Receipts	Payments	Cash surplus(b)
1988-89	88,369	82,202	6,167	4177	6035	257	91544	87188	6424
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	186,971	178,935	8,036	na	na	1,575	na	na	9,611
2004-05(e)	202,662	193,441	9,221	na	na	1,288	na	na	10,509
2005-06(e)	**214,515**	**205,132**	**8,921**	**na**	**na**	**433**	**na**	**na**	**9,354**
2006-07(p)	221,891	213,015	7,933	na	na	na	na	na	na
2007-08(p)	232,525	223,029	8,500	na	na	na	na	na	na
2008-09(p)	244,245	233,907	9,284	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.
(b) These items exclude expected Future Fund earnings. Expected Future Fund earnings are shown in Table 1.
(e) Estimates.
(p) Projections.
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(b)	Fiscal balance(b)	Revenue	Expenses	Fiscal balance	Revenue	Expenses(b)	Fiscal balance(b)
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	166,875	156,209	11,892	25,485	23,542	1,062	188,412	174,646	12,953
2000-01	161,789	157,382	5,575	25,869	24,762	-826	183,052	177,538	4,750
2001-02	162,599	166,401	-3,433	26,638	25,341	793	184,629	187,134	-2,640
2002-03	175,191	170,676	4,734	24,339	22,916	1,975	194,402	188,507	6,709
2003-04	187,559	182,005	4,830	25,449	23,444	2,143	207,263	199,705	6,973
2004-05(e)	202,666	195,012	7,003	26,693	24,924	1,475	224,395	214,972	8,478
2005-06(e)	**214,511**	**206,081**	**7,410**	**27,778**	**26,886**	**213**	**236,778**	**227,456**	**7,623**
2006-07(p)	222,882	214,806	7,458	na	na	na	na	na	na
2007-08(p)	233,405	225,400	8,003	na	na	na	na	na	na
2008-09(p)	245,326	236,568	9,022	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) The increases in expenses and decreases in fiscal balance and net worth arise from a change in recognition of family tax benefits and other expenses from a cash to an accrual basis.
(e) Estimates.
(p) Projections.
na Data not available.

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