

## 2015-16 WA State Budget

**BUDGET OVERVIEW****Key Points**

- Forecast deficit of \$1.3billion in 2014-15 with revenues hit by reduced royalties and low GST distribution.
- First deficit in 15 years.
- Net debt set to reach \$36billion by 2017-18.
- ‘Lagged’ GST receipts to help deliver a return to surplus in 2017-18.
- New asset sales foreshadowed, including Fremantle Port.

**SUMMARY AND ANALYSIS**

As predicted in the Government’s Mid-Year economic review, the seventh budget of the Barnett Government has confirmed that Western Australia is set to record its first budget deficit in 15 years. Treasurer Dr Mike Nahan described the budget as being prepared “in the most challenging economic and fiscal environment the State has faced in at least the last three decades”, and this is certainly reflected in the budget aggregates.

Treasurer Nahan has revealed the extent of the State’s declining fortunes with revenue written down by \$10.2billion since the previous budget. This in turn has fuelled an increase in State debt, which is now expected to peak at an unprecedented \$36billion. The recently announced \$499million injection of Federal funding for WA road projects has not been included in the budget figures, but would provide some offset.

Since the December 2014 Mid-Year review revenue forecasts have been hit by reductions in royalties, payroll tax, land tax and motor vehicle stamp duty. New revenue measures, including increases in land tax rates, only go a small way to mitigating the losses. The State will begin to see some improvement in GST payments as the lagged Commonwealth Grants Commission process kicks in, but deficits are unavoidable for the next few years. While much has been made of WA’s GST relatively falling to only 30 cents in the dollar, Treasury now estimates that this will recover to 67 cents by 2018-19 as the lagged payments flow.

The State’s revenue dilemma has been exacerbated by the Government’s ongoing capital works program, which is still worth around \$6billion each year. Since the Mid-Year review the program has increased by a further \$1.3billion across the period 2014-15 to 2017-18.

The Government has announced an expanded asset sales program to tackle the debt problem, including the sale of Fremantle Port, which will include the previously announced Kwinana Bulk Terminal. No significant sales have been concluded since the Premier first flagged privatisations in response to a credit rating down grade in September 2013. The lack of action has contributed to ratings agencies criticising the Government for a ‘lack of political will’, and this position is unlikely to change until firm action is seen.

Treasurer Nahan has managed to keep recurrent expenditure growth to just 4 per cent in 2014-15, though this is higher than the original budget target of 2.6 per cent. He will have to do even better to meet the forecast rate of 2.5 per cent in the year ahead, and then 2.1 per cent in the election year of 2016-17.

As reported in the media, a no-fault insurance scheme is set to be funded through a \$99 levy on most motor vehicles. The accounting treatment of the fund means that this will have a positive benefit on the State's finances, reducing net debt by \$286million in 2019.

In some rare good news for the resources sector, the Government appears to have scrapped planned royalty rate changes that were proposed by former Treasurer Christian Porter. This move will cost the Government \$560million in foregone revenue.

After pushing back a planned increase in the payroll tax exemption threshold to 2017 in the Mid-Year Review, the Government has now reversed this decision, reinstating the original commencement date of 1 July 2016, which will benefit around 17,000 small businesses.

Similarly, a previous announcement that the metropolitan region improvement tax would be extended State-wide has been scaled back to only Bunbury and the Peel regions, resulting in a revenue reduction of around \$96million over four years.

Despite the deterioration of the finances, the Government has sought to shield households from the impact. The estimated impact of budget measures on Treasury's 'representative household' shows a modest 3.8 per cent increase in fees and charges, equating to an extra \$198 per year.

This includes:

- electricity charges up 4.5 per cent;
- water, sewage and drainage up 4.5 per cent; and
- CTP insurance up 4.1 per cent (does not include no-fault insurance increase, as this takes effect from 1 July 2016).

### **Savings and Revenue Measures**

In an attempt to limit the impact of the revenue reductions the Government has announced another round of savings and revenue measures, which are expected to total \$1.3billion. The most significant measure is an adjustment to land tax rates, the third such change in three years. New measures include:

- removal of the 'cellar door subsidy' (+\$11million);
- removal of the first home owner grant for establish homes (+\$109million);
- savings resulting from 'expenditure reviews' of several Government agencies (+\$137million);
- revisions to the land tax scale (+\$826million);
- an increase in the loan guarantee fee for local governments, Universities and KeyStart (+\$24million); and
- reforms to social concessions (+\$199million).

The flagged reforms to social concessions include a freeze on the rate of the Cost of Living Rebate, a means-tested energy assistance payment and a cap on local council and water service rebates.

## New Expenditure

Reflecting a desire to contain expenditure growth, there are limited new expenditure measures in this year's budget. New recurrent expenditure includes:

- \$417million in hospital activity funding for WA Health;
- \$172million for core child protection services;
- \$122million in the operating subsidy paid to the Public Transport Authority;
- \$26million to the Mental Health Commission over the next four years for a new Suicide Prevention Strategy;
- \$16million in 2015-16 to address high-priority maintenance issues in schools; and
- \$20.5million for events funding.

New capital investments announced as part of the budget include:

- \$308million as part of a \$560million new Social Housing Investment Package;
- \$191million over four years for school infrastructure;
- \$140million in 2015-16 for Western Power, primarily for wood pole and electrical conductor management programs;
- \$22million over three years for the New Women's Custodial Centre; and
- \$16million for the Public Transport Authority to replace escalators at the Perth Underground and Esplanade train stations, and a further \$19 million for the Transperth Rail Resilience Package.

## Asset Sales

To counter ballooning State debt, the Government has announced a "significant expansion" of the State's asset sales program. Key features of the program include:

- the disposal, through a long term lease, of the assets and operations of the Fremantle Port Authority (replacing the separate sale of the Kwinana Bulk Terminal);
- sale of the TAB;
- identification of additional assets for consideration, including:
  - the Forest Products Commission;
  - a portfolio of Government Regional Officer Housing stock;
  - securitisation of part of KeyStart's loan book;
  - the State's vehicle fleet, via a sale and leaseback arrangement;
  - various Government-owned office buildings, via a sale and leaseback arrangement; and
  - individual generation assets of Synergy and Horizon Power, and Western Power's non-core assets.

No revenue has yet been booked by the Government, and proceeds of any sales will not be reflected until they are completed. Further benefit may be obtained through the Commonwealth's Asset Recycling Scheme, though the priority for the State will be debt reduction rather than new investments.

## Government Trading Enterprises

Reforms of the State's government trading enterprises also continue. The Water Corporation is set to shift its focus from building new infrastructure to operating and maintaining existing assets,

which has seen its investment program reduced by \$403million and operating subsidy cut by \$139million since last year's Budget.

Synergy too has identified business efficiencies worth \$450million over the forward estimates, which is on top of previously announced merger savings and a similar reduction in the organisations operating subsidy in December. Combined, these measures mean that the operating subsidy has been reduced by a total of \$971million since the 2014-15 Budget.

Horizon Power has also identified a further \$40million in savings across the forward estimates through internal process improvements.

## KEY BUDGET DATA AND FORECASTS

The following table summarises key Budget data:

<b>KEY BUDGET AGGREGATES</b>							Table 1
Western Australia							
	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	
	Actual	Estimated Actual	Budget Estimate	Forward Estimate	Forward Estimate	Forward Estimate	
<b>GENERAL GOVERNMENT SECTOR</b>							
<b>Net Operating Balance (\$m)</b>	<b>719</b>	<b>-1,287</b>	<b>-2,708</b>	<b>-1,148</b>	<b>874</b>	<b>2,209</b>	
Revenue (\$m)	27,956	27,045	26,325	28,496	31,075	33,517	
Revenue Growth (%)	8.7	-3.3	-2.7	8.2	9.0	7.9	
Expenses (\$m)	27,236	28,332	29,033	29,644	30,201	31,308	
Expense Growth (%)	6.9	4.0	2.5	2.1	1.9	3.7	
<b>TOTAL PUBLIC SECTOR</b>							
Net Debt at 30 June (\$m)	20,754	25,455	30,996	34,443	36,289	35,753	
Asset Investment Program (\$m)	6,814	6,555	6,284	5,963	6,081	5,757	
Cash Position (\$m)	-2,465	-4,140	-5,090	-3,139	-1,147	790	
Gross Borrowings at 30 June (\$m)	41,216	44,510	46,830	49,766	52,774	54,860	
<b>KEY FINANCIAL RATIOS <sup>(a)</sup></b>							
Cash Operating Surplus as a Share of Receipts (%)	7.5	2.1	-0.6	3.0	6.7	9.5	
Net Debt to Revenue (%)	55.2	67.9	80.5	83.3	81.8	75.4	

(a) These ratios relate to the total non-financial public sector.

*Source: Department of Treasury 2015-16 Budget Papers*

## WA Economy - Budget Assumptions

To populate estimates of revenue and expenditure, the Department of Treasury builds assumptions into its modelling. These estimates provide a good insight into expectations of economic activity in the years ahead and can have a considerable impact on the final Budget numbers.

Real gross state product is expected to drop to just 2 per cent in 2015-16, while State Final Demand is not expected to return to positive growth until 2017-18. This is reflected in declining

business investment across all years as the mining boom continues to wind down and a reduced likelihood of existing planned (but yet to commence) projects proceeding in the short to medium-term.

As evidenced by the reduction in forecast royalty revenues, Treasury assumptions for the iron ore price show no return to the high prices of previous years, with only a moderate price recovery to \$US61.8/tonne CFR. Every \$US1 per tonne reduction in the iron ore price cuts approximately \$70million from the State's royalty revenue.

In line with the three-year rolling average methodology of the Commonwealth Grants Commission, the reduction in iron ore royalties is somewhat offset by increased GST revenue. For every \$100million decrease in iron ore royalties the State can expect to be compensated by \$86million in GST revenue, albeit with a multi-year time lag.

Table 3

## KEY BUDGET ASSUMPTIONS Western Australia

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
	Actual	Estimated Actual	Budget Estimate	Forward Estimate	Forward Estimate	Forward Estimate
Real Gross State Product growth (%)	5.5	3.25	2.0	3.5	2.75	2.75
Real State Final Demand growth (%)	-2.2	-2.5	-1.25	0.0	1.0	2.0
Employment growth (%)	1.1	2.5	1.75	1.75	2.0	2.0
Unemployment rate (%) <sup>(a)</sup>	4.8	5.5	6.25	6.0	5.75	5.25
Wage Price Index growth (%)	2.8	2.25	2.75	3.0	3.25	3.5
Perth Consumer Price Index growth (%)	3.0	2.0	2.25	2.5	2.5	2.5
'Headline' iron ore price (\$US/tonne CFR)	122.8	68.8	47.5	50.7	56.3	61.8
Iron ore volumes (million dry tonnes)	632	716	748	772	797	799
Crude oil price (\$US per barrel)	109.4	75.1	64.2	68.2	70.4	71.9
Exchange rate (US cents)	91.8	83.3	75.9	75.0	74.3	73.9
Population growth (%)	2.6	1.9	2.0	2.1	2.2	2.2
Interest rate assumptions (%):						
- Public Bank Account interest earnings <sup>(a)</sup>	2.8	2.6	2.1	2.1	2.1	2.1
- Consolidated Account borrowings <sup>(a)</sup>	4.0	3.9	3.4	3.2	3.1	3.1

(a) Average rate over the year.

*Source: Department of Treasury 2015-16 Budget Papers*

### RESPONSES TO THE BUDGET

- Opposition Leader Mark McGowan has said "Colin Barnett has blown the budget and now he's making WA families pay for it". Mr McGowan goes on to say "what have we got to show from the resources boom? Record debt and deficit and rising unemployment. That's Colin Barnett's real legacy to WA."
- Shadow Treasurer Ben Wyatt has savaged the Budget, labelling Premier Barnett as "the worst manager of State finances WA has ever seen" and stating "the tragedy is that Western Australia emerges from one of the greatest periods of revenue increases it has ever seen with a balance sheet crippled by record debt with no believable path to stabilisation".
- The MUA secretary Chris Cain has labelled plans to privatise Fremantle Port as a "disgrace" and vowed to fight any sale, claiming the issues has the potential to bring down the Government.



- REIWA President David Airey has described the loss of the \$3,000 first home owner grant as a significant blow that would promote urban sprawl.
- Joe Lenzo of the Property Council of Australia has taken aim at the third consecutive increase in land tax, saying that “many owners of medium to lower priced properties will be hit by huge and unprecedented land tax increases”.
- The WA Council of Social Service has welcomed additional funding for social housing and the introduction of a no-fault insurance scheme, but said that the budget failed to prevent growth in demand for acute care.
- The WA Chamber of Commerce and Industry has supported the Government’s asset sales program, but is disappointed in the increases in land tax and the lack of public sector reform.
- UnionsWA secretary Meredith Hammett has criticised the budget priorities, stating “average working people will be paying much for the services that they rely on like transport, electricity, water - leading them worse off on every occasion they pay a bill.”
- Confirmation that royalty rates would not be increased has been welcomed by the Chamber of Minerals and Energy.
- Health Services Union secretary Dan Hill has claimed the Health Minister Kim Hames is ‘missing in action’ and that the unsustainable health budget would result in job losses.
- It is reported that rating agency Standard and Poor's has at this point retained its current WA credit rating of AA+ with a negative watch.

### **FURTHER READING**

2015-16 State Budget Papers – [www.ourstatebudget.wa.gov.au](http://www.ourstatebudget.wa.gov.au)