

2016-17 WA State Budget

BUDGET OVERVIEW

Key Points

- Record \$3.9billion deficit forecast for 2016-17, following revenue write-downs of \$14.7billion since the 2014-15 Budget.
- Worst set of Budget figures in State's history.
- State debt will reach \$33billion next year and grow to more than \$40billion by 2019-20.
- Budget will not return to surplus until 2019-20.
- State Final Demand (the WA domestic economy) is forecast to contract by 3.75 per cent in 2016-17 following a 4.25 per cent decline this year and 3.6 per cent decline in 2014-15.
- Government will take asset sales program to the next election with the aim of raising \$16billion, including proceeds from the sale of Western Power and Horizon's Pilbara assets.

SUMMARY AND ANALYSIS

Treasurer Mike Nahan's third and the Barnett Government's eighth budget makes for grim reading as the State records the worst set of financial figures in WA's history. It's the Government's last budget before next March's State Election.

Dr Nahan revised down the Budget deficit forecast for this year from \$3.1billion to \$2billion. However the deficit will balloon to a record \$3.9billion in 2016-17 as the State's decline in revenue and weak GST receipts bite hard into the State's financial position.

The Budget forecasts five successive deficits (since 2014) totalling more than \$6.6billion before a return to surplus in 2019-20.

State debt is expected to exceed \$40billion by 2019-20 with the State's debt to revenue ratio now expected to peak at 95.3 per cent. Non-commercial or general Government sector debt is expected to reach \$25.4billion by 2020.

WA's Gross State Product will grow by just 1.25 per cent next year, but State Final Demand (which excludes exports) will shrink by 3.75 per cent, reflecting declining business investment at the end of the resources boom.

Crucially for the Government's re-election chances, unemployment is forecast to peak at 6.75 per cent in the election year.

Alarming, the domestic economy may be even weaker than Treasury forecasts, with the Budget papers stating:

“A key risk to the economic outlook is the magnitude and timing of expected declines in business investment, which has flow-on implications for the timing of exports, and the outlook for labour demand and population growth.

“The business investment forecasts include the assumption that some prospective major projects will be approved or that currently unidentified projects will emerge across the forecast period. However, if this does not occur, the declines in investment may be larger than forecast.

“The large volume of new dwellings under construction at a time when the established housing market has substantial spare capacity, and in the context of slowing population growth, means there is a heightened risk of over-supply in the housing market”.

The Treasurer described the revenue collapse as *“unprecedented in the State's history”* and *“the mother of revenue hits”*.

Revenue estimates have been written down by a total of \$14.7billion or 12 per cent (over the period 2014-15 to 2017-18) since the 2014-15 Budget. Revenue is expected to be \$810million or 3.1 per cent lower in 2016-17 than in 2015-16 – the third consecutive year of declining revenue.

Dr Nahan declared that the Turnbull Government would suffer at the Federal election in WA as voters reacted to Canberra's failure to fix the GST distribution system and boost payments in the one-time boom State.

The Treasurer said WA's GST grant would be equal to just 30.3 per cent of its population share in 2016-17:

“Our state revenue has taken the biggest hit to any Government since the Great Depression.”

Household charges will rise by 4.8 per cent or \$257 per year for the average household. Water will increase by 4 per cent, while electricity charges will increase by 3 per cent. The 4.8 per cent rise in household fees and charges is more than two and a half times the forecast 1.75 per cent CPI rate.

Despite rising debt and deficit, the Government will not increase taxes and the State's public sector hiring freeze has come to an end. The Government will invest very modestly in tourism, agriculture, innovation and shipbuilding as it seeks to diversify the WA economy following the collapse in iron ore mining receipts.

ASSET SALES

The Government will take the argument for privatisation to the next election as it seeks a path to debt reduction over the medium-term.

Key features of the privatisation program include:

- The sale of Western Power – which the Government projects will raise \$12billion.
- Sale of Horizon Power's Pilbara poles and wire assets valued at \$800million.
- Disposal of Utah Point Bulk Handling facility.

- Long-term lease of Fremantle Port.
- Land Asset Sales Program.
- Sale of the TAB.
- Additional assets for consideration, include:
 - Securitisation of part of KeyStart's loan book;
 - The State's vehicle fleet, via a sale and leaseback arrangement; and
 - Sale of Insurance Commission of Western Australia's property portfolio.

No revenue has yet been booked by the Government, and proceeds of any sales will not be reflected until they are completed.

The priority for the State will be debt reduction rather than new investments.

Dr Nahan said \$11billion out of the expected \$16billion in proceeds from the sale assets would be used to pay down debt from construction of the Perth Airport Link, the new stadium, hospitals and schools. The other \$5billion would go towards a new infrastructure fund.

However, the Fremantle Port sale is going nowhere after the Nationals made their opposition clear and there is no certainty Western Power will be an easy sell either.

The Nationals are yet to decide if they will support it and Labor and the unions will make it a central theme of the State election campaign.

SALARIES, EXPENSES AND WAGES POLICY

The Treasurer has delivered commendably low expense growth figures of 2.2 per cent in 2014-15 and a forecast 2.5 per cent in 2015-16, but expenses are expected to growth by 3.7 per cent next year. The forecast for the following year is minus 0.1 per cent which is scarcely believable.

The last time WA spent less in one year on the public sector than it did the previous year was 1994 when then Premier Richard Court was cleaning up the mess of WA Inc.

Growth of salaries expenditure is forecast to decline but not just yet - with growth of 3.5 per cent in 2016-17 and 1.7 per cent per annum across the forward estimates.

Wages policy of only 1.5 per cent per annum will test the Government with agreements to be renegotiated for prison officers, registered nurses, health salaried officers, doctors, public servants and police officers over the next 15 months.

A 3.5 per cent savings target will apply to a further 54 agencies. This is expected to deliver savings of \$461million over the period 2017-18 to 2019-20, with specific savings measures for each affected agency to be detailed in the 2017-18 Budget.

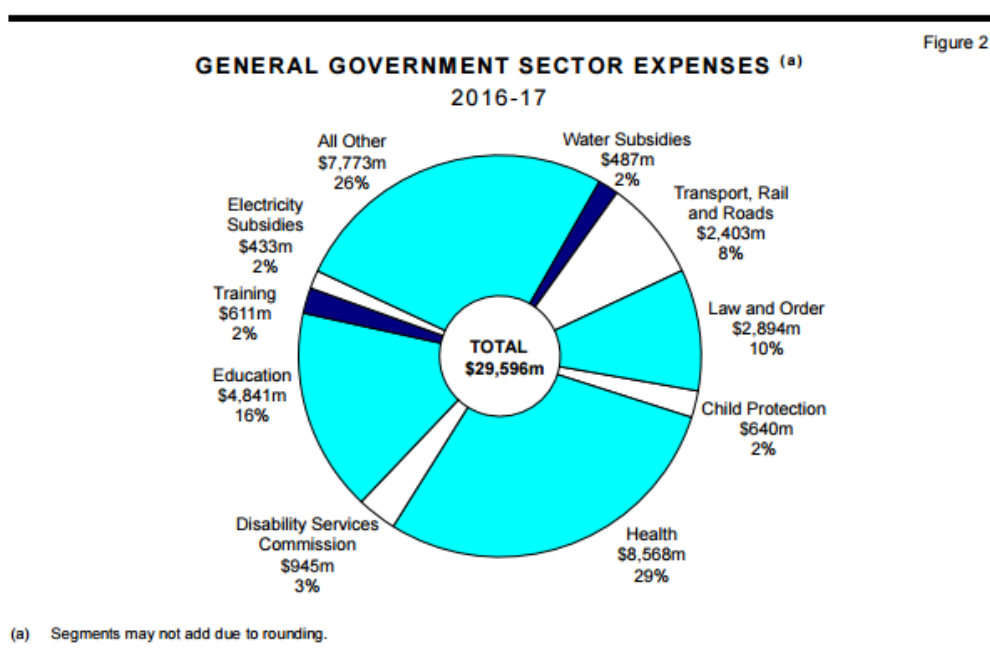
This is only the latest of an extensive series of savings measures which have been imposed across the board since 2013. It is doubtful if much more can be extracted from departments without actually sacrificing whole programs.

It is worth noting that the savings target is general with specific agency measures not to be detailed until next year's Budget following the election.

EXPENDITURE

The 2016-17 Budget takes a cautious approach to spending, with general Government expenses revised down by \$745million (over the period 2015-16 to 2018-19) since the Mid-year Review.

Savings from the Government's new wages policy, a roll-out of Agency Expenditure Reviews and other cost reductions offset new spending initiatives.



Source: Department of Treasury 2016-17 Budget Papers

New spending initiatives in this Budget are focused on modest initiatives (roughly \$100million over four years) to broaden the economy and create new job opportunities in areas like tourism, agriculture and fisheries.

These include:

- \$47million for Tourism.
- \$20million for Government departments to support research, innovation and start-ups.
- \$16million for the film industry.
- \$7million for biodiversity research and \$6million for minerals research.
- \$4million for aquaculture infrastructure.

New spending on services includes:

- \$26million for expansion of National Disability Insurance Scheme (NDIS) trials.
- \$147million extra over four years to meet growth in the State's prisoner population.
- \$14.9million over two years for a new methamphetamine strategy.

General Government expenses are forecast to increase by an average of 2.4 per cent over the period 2016-17 to 2019-20. Spending on health (up \$1,104million or 13.5 per cent) and education (up \$527million, or 11.1 per cent) makes up nearly 60 per cent of the projected growth in spending between 2015-16 and 2019-20.

Overall, health spending equates to \$8.568b or 29 per cent of this year's Budget.

The Government has abandoned its 2015 policy to shift WA hospital costs to the national projected average price by 2020-21. The gap between WA and national costs in 2014, originally estimated at 10.3 per cent, is now known to be 17.8 per cent and even if the original, but now undeliverable, price path was achieved would still be 9.2 per cent in 2020-21.

The revised policy is to limit growth in health costs to the public sector wages policy of 1.5 per cent per annum with savings from reductions in health's non-hospital costs to be reinvested in the hospitals. There is a very significant risk that these Budget settings will not be delivered.

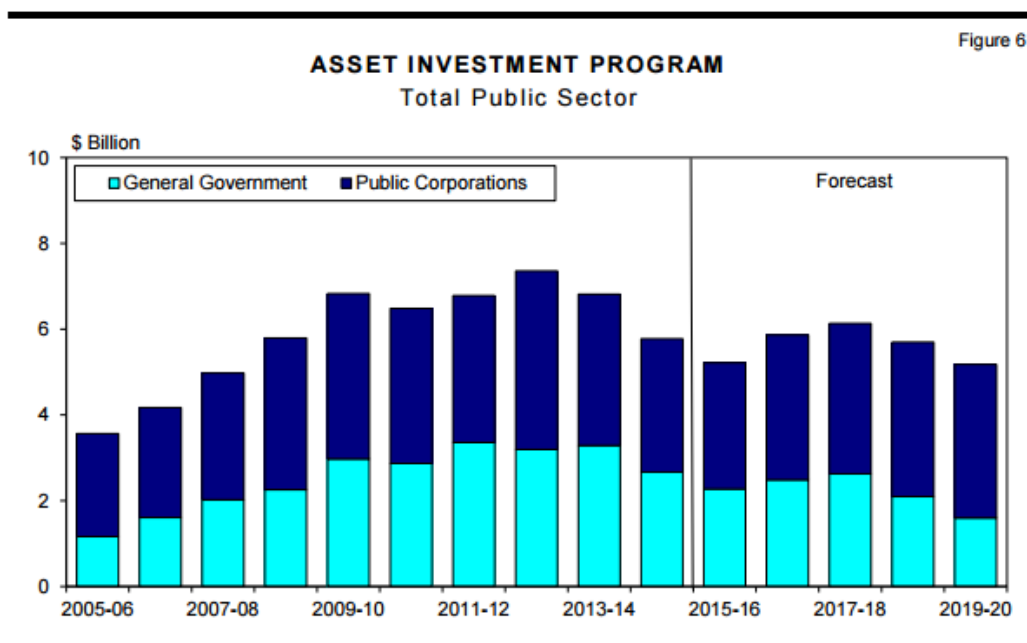
Electricity, water and public transport subsidies total an estimated \$1.8billion in 2016-17 - \$329million for the general electricity tariff subsidy and \$320million for country water subsidies.

Asset Investment Program

The \$5.862billion Asset Investment Program is mainly devoted to continuing expenditure on already announced projects such as the Forrestfield Airport Link, the Perth Freight Link and North Link.

New initiatives include:

- \$49 million for a dedicated bus lane to Ellenbrook.
- \$145 million over four years to construct a seven-kilometre dual carriageway on Armadale Road.
- \$300.4million for new senior high schools and primary schools.



KEY BUDGET DATA AND FORECASTS

The following table summarises key Budget data:

Table 2

KEY BUDGET AGGREGATES						
Western Australia						
	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
	Actual	Estimated Actual	Budget Estimate	Forward Estimate	Forward Estimate	Forward Estimate
GENERAL GOVERNMENT SECTOR						
Net Operating Balance (\$m)	-431	-2,037	-3,914	-1,893	-197	1,086
Revenue (\$m)	27,400	26,492	25,681	27,672	30,305	32,481
Revenue Growth (%)	-2.0	-3.3	-3.1	7.8	9.5	7.2
Expenses (\$m)	27,831	28,529	29,596	29,565	30,502	31,394
Expense Growth (%)	2.2	2.5	3.7	-0.1	3.2	2.9
TOTAL PUBLIC SECTOR						
Net Debt at 30 June (\$m)	23,374	27,860	33,838	38,258	40,040	40,193
Asset Investment Program (\$m)	5,777	5,212	5,862	6,134	5,698	5,175
Cash Position (\$m)	-2,500	-4,301	-5,526	-3,700	-1,516	147
Gross Borrowings at 30 June (\$m)	44,252	49,821	53,424	56,167	60,731	63,625
KEY FINANCIAL RATIOS ^(a)						
Cash Operating Surplus as a Share of Receipts (%)	5.1	-0.5	-2.2	2.1	5.3	7.3
Net Debt to Revenue (%)	61.4	77.5	91.2	95.3	92.4	88.2

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

The following table summarises Treasury's economic forecasts:

Table 1

KEY BUDGET ASSUMPTIONS						
Western Australia						
	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
	Actual	Estimated Actual	Budget Estimate	Forward Estimate	Forward Estimate	Forward Estimate
Real Gross State Product (%)	3.5	1.0	1.25	2.5	2.5	3.0
Real State Final Demand (%)	-3.6	-4.25	-3.75	-0.25	1.0	3.25
Employment growth (%)	1.5	0.25	0.25	0.75	1.5	2.0
Unemployment rate (%) ^(a)	5.4	6.25	6.75	6.50	6.25	5.75
Wage Price Index growth (%)	2.2	1.75	1.75	2.25	2.75	3.25
Perth Consumer Price Index growth (%)	1.8	1.25	1.75	2.25	2.5	2.5
Population growth (%)	1.4	1.2	1.3	1.5	1.7	1.9
\$/US/\$A exchange rate (cents)	83.6	73.3	75.7	74.7	73.8	73.0
Iron ore price (\$US/tonne CFR) ^(b)	71.1	50.9	47.7	49.2	51.6	54.0
Iron ore volumes (million dry tonnes)	715	765	782	803	814	817
Crude oil price (\$US/barrel)	73.5	41.1	44.4	47.1	49.1	50.9
Interest rate assumptions (%)^(a)						
- Public Bank Account earnings	2.8	2.3	1.8	1.8	1.9	2.0
- Consolidated Account borrowings	3.9	3.5	3.2	3.2	3.3	3.4

(a) Average rate over the year.

(b) The Steel Index (TSI) benchmark spot price for ore with 62% iron content delivered to China, including cost and freight (CFR).

Source: Department of Treasury 2016-17 Budget Papers

RESPONSES TO THE BUDGET

Opposition Leader Mark McGowan declared the Budget a “*financial wreck*” and attacked the Treasurer for delivering a Budget of “*shaky privatisations and job losses*”.

“This is a Budget of desperation, they have run out of ideas, run out of energy, they have no plan for the future.”

Shadow Treasurer Ben Wyatt attacked the Government calling it “*a tired Budget from a tired Government*” and said it confirmed “*the Liberal Party spent without constraint during the economic good times*”.

Ratings agency Moody’s said WA’s medium-term Budget deficits were credit negative and the State’s fiscal deterioration reflected significant slowing in economic growth.

Moody’s added that the Treasurer’s efforts were not sufficient to stem budgetary gaps which would lead to further increases in the State’s debt burden.

CSA Secretary, Toni Walkington said, “*The Treasurer announced today another 54 government agencies would be subject to expenditure reviews.*”

“Review is just another word for cuts. He wants to cut \$461million over the next three years from critical public services”.

The Tourism Council has welcomed the overturning of cuts to WA’s tourism marketing funding for 2016-2017.

“We are pleased the government hasn’t implemented cuts in 2016-17, despite tough Budget circumstances, and has provided good consistent funding for PCB into the future,” said Tourism Council WA chief executive officer Evan Hall.

WA Council of Social Service (WACOSS) CEO, Irina Cattalini said the Budget did not chart a sustainable path back to surplus.

“We need to invest more in social services to reverse the alarming growth in high cost, acute services like prisons, hospitals and child protection if we are going to achieve a sustainable budget and service system.”

The Australian Medical Association has welcomed the end of the freeze on hiring public servants announced in the Budget.

Chamber of Commerce and Industry WA CEO Deidre Willmott gave the Budget the green light stating it gave a vision for growth, spending restraint, asset sales and no new taxes.

FURTHER READING

2016-17 State Budget Papers – www.ourstatebudget.wa.gov.au