Wednesday, 2 May 2018

Victorian State Budget 2018-19

When You've Got It, Spend It

- **The Victorian Government handed down its 2018-19 Budget yesterday.**
- **Expectations for strong revenue growth have paved the way for a big increase in spending. Revenue strength has largely been a result of the upswing in the property market, firm jobs growth, fast population growth and a robust Victorian economy.**
- **As in recent years, infrastructure spending continued to be a key feature of the Budget. Infrastructure spending is set to hit a record of $13.7 billion in 2018-19. Infrastructure spending has provided major support to the Victorian economy, creating positive spillovers for the private sector. The ongoing spending on infrastructure will continue to boost economic activity, jobs and productivity over the long term, helping to improve the operating backdrop for businesses.**
- **The Government has also placed skills and training at the centrepiece for this year's Budget. The big winners were education and healthcare, but there were also increases to spending for a raft of other measures.**
- **Businesses based in regional Victoria were winners with the government cutting back country payroll taxes to half the metropolitan rate.**
- **The direct impact from stronger government spending adds to economic activity in the State. The aim to address skills should further add to productivity, by boosting workforce participation and potential growth in the economy.**
- **The Government's fiscal position is strong, supported by strong economic growth in the State. An operating surplus of $1.4 billion is estimated for 2018-19. This surplus is expected to increase to $2.9 billion in 2021-22.**
- **Good times will not last forever. A slowdown in the housing market will be the biggest test to the fiscal position in coming years. Fortunately, Victoria's economy has been supported by strong population growth, an infrastructure spending boost, and an upswing in the global economy, which suggests Victoria's fiscal position should remain in good shape.**
- **We expect Victoria to retain its triple-A credit rating.**

The Victorian Government handed down its 2018-19 Budget yesterday. Ahead of an election and amid strong economic activity in the State, it was no surprise that it was a Budget with giveaways.

Expectations for strong revenue growth, particularly for 2018-19, have paved the way for a big increase in spending. Revenue strength has largely been as a result of the upswing in the property market, which has boosted land transfer duty and other property taxes. These comprise a large chunk of the State coffers. Additionally, firm population growth, the health of the labour market and the economy has boosted other areas of tax revenue.

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Despite the increases to spending, the forecast strength in revenue growth is expected to allow the State government to deliver a surplus of $1.4 billion in 2018-19, after an expected $2.0 billion in 2017-18. The size of the surplus is expected to gradually increase over the projected years to 2021-22.

Good times will not last forever. A slowdown in the housing market will be the biggest test to the fiscal position in coming years. While the State government acknowledges a moderation in housing conditions, the slowdown suggests that the current pace of revenue growth is unlikely to be repeated in coming years. Fortunately, Victoria's economy has been supported by strong population growth, an infrastructure spending boost, and an upswing in the global economy, which suggests Victoria's fiscal position should remain in good shape. Victoria should retain its triple-A credit rating.

Economic Impact

The impact from stronger government spending adds to economic activity in the State. Infrastructure spending has been a major support to the Victorian economy, which has created positive spillover effects for the private sector. The ongoing spending on infrastructure will continue to boost economic activity, jobs and productivity over the long term.

The aim to address skills should further add to productivity, by boosting workforce participation and potential growth in the economy.

What does it mean for Businesses?

Businesses in regional Victoria were the key beneficiaries of direct measures. Businesses based in regional Victoria can bank on tax relief, with the government cutting back country payroll taxes to half the metropolitan rate. The tax cut will apply to businesses based outside Melbourne who pay at least 85% of their payroll tax to regional employees will be eligible for the lower rates. The Victorian Treasury forecasts that about 4,000 existing businesses in regional Victoria will benefit from the cut.

The obvious other winners were education, training sectors and healthcare. Additionally, selected training courses, which will become free of charge, could address skilled shortages and skilled mismatches for those industries linked to these courses.

More generally, the infrastructure spending boost and the support to the economy are key positives for all businesses. The boost to infrastructure lifts economic activity, improving the economic backdrop and business environment for businesses.

What does it mean for Consumers?

There were some measures aimed at alleviating the cost of rising power bills. It includes the Budget committing $47.8 million to pay consumers to visit an energy comparison website.

Incentives and taxes related to the housing sector were left untouched.

Economic Forecasts

After economic growth of 3.5% in 2015-16 and 3.3% growth in 2016-17, the expectation for 2.75% economic growth in 2018-19 and later years is conservative.

Table 2.1: Victorian economic forecasts[a] **(per cent)**

	2016-17 actual	2017-18 forecast	2018-19 forecast	2019-20 forecast	2020-21 projection	2021-22 projection
Real gross state product	3.3	3.00	2.75	2.75	2.75	2.75
Employment	3.9	2.75	2.00	1.75	1.75	1.75
Unemployment rate [b]	5.9	5.75	5.75	5.50	5.50	5.50
Consumer price index [c]	1.9	2.00	2.25	2.50	2.50	2.50
Wage price index [d]	2.0	2.25	2.50	2.75	3.00	3.25
Population [e]	2.3	2.30	2.20	2.10	2.00	2.00

Sources: Department of Treasury and Finance; Australian Bureau of Statistics.

The Government also expects the unemployment rate to stand at 5.75% in 2018-19 and to fall to 5.5% in 2019-20, corresponding to employment growth of 2.0% and 1.75% in respective years. The latest available data shows that employment grew by 2.4% in the year to March in Victoria. So these Budget forecasts imply a moderate slowing in employment growth over coming years. These assumptions are plausible and also conservative.

The key downside risk for the Victorian economy and taxation revenue is the housing slowdown currently underway. The positive impact on economic activity from housing construction and household spending is waning. These more conservative forecasts perhaps acknowledge these potential risks to the outlook.

Government revenues are highly dependent on activity in the housing sector. Nearly 30% of taxation revenues come from transfer duties.

The ongoing solid rates of population growth suggest some upside risk to the Government's economic growth forecasts. In addition, the strength of the labour market will be supportive of other sources of revenue, including payroll tax. And business investment should become a bigger driver of economic growth and contribute to revenue growth.

Table 1.1: General government fiscal aggregates[a]

	Unit of measure	2016-17 actual	2017-18 revised	2018-19 budget	2019-20 estimate	2020-21 estimate	2021-22 estimate
Net result from transactions	$ billion	2.7	2.0	1.4	2.0	2.7	2.9
Government infrastructure investment	$ billion	9.1	11.6	13.7	10.0	8.9	7.6
Net debt	$ billion	15.8	19.6	24.3	28.0	29.8	31.4
Net debt to GSP	per cent	3.9	4.6	5.4	5.9	6.0	6.0

Source: Department of Treasury and Finance

Budget Position

The Government's fiscal position remains healthy supported by strong economic growth in the State. An operating surplus of $1.4 billion is estimated for 2018-19, down from an estimated $2.0 billion in 2017-18. The operating surplus is projected to increase to $2.9 billion in 2021-22.

Net debt is projected to lift to 5.4% of Gross State Product in 2018-19 and rise to 6.0% in 2020-21.

Victoria holds a triple-A credit rating from both Standard & Poor's and Moody's. We do not anticipate this credit rating to be at risk after this Budget.

Key Measures in the Budget

Infrastructure

Infrastructure has continued to be a key focus of the Budget. On top of previously announced projects, additional spending announced this year includes:

- $3.3 billion for upgrades and widenings, including $110 million for the North East Link
- $1 billion for metropolitan pubic transport upgrades
- $941 million for regional roads
- $704 million on regional public transport

Education, Skills and Training

Building skills is one of the key priorities in this year's Budget. These include:

- $172 million to make 30 priority TAFE courses and 18 pre-apprenticeship courses free
- $303.8 million for 30,000 new training places
- Over $120 million to upgrade TAFE campuses
- $49.8 million for a new Head Start Apprenticeships and Traineeships program
- $$434 million to upgrade schools, $353 million to build new schools and $272 million for land for new schools

Health

- $2.1 billion for more paramedics, ambulance vehicles, hospital admissions, emergency treatments and elective surgeries
- $1.2 billion to build and expand hospitals
- $705 million to support mental health services, which includes extra regional rehabilitation facilities and new emergency department crisis hubs

Regional Victoria

- The payroll tax rate for regional businesses will be reduced from 3.65% to 2.425% for regional businesses, adding to broader reductions to payroll tax in previous Budgets
- Doubling the stamp-duty-free threshold from $300,000 to $600,000 for those buying their first farm

Safety

- Increasing investment for police and improving infrastructure for the State's prison system
- $49.9 million to support victims of family violence

Creative Arts and Leisure

- $82.7 million to support galleries, museums and the creative sector
- $231 million to redevelop sporting venues including Etihad Stadium, updating the National Sports Museum at the MCG and upgrades to Whitten Oval and Eureka Stadium
- $242 million to upgrade suburban grounds and support local clubs

Contact Listing

Chief Economist	Senior Economist	Senior Economist
Besa Deda dedab@bankofmelbourne.com.au (02) 8254 3251	Josephine Horton hortonj@bankofmelbourne.com.au (02) 8253 6696	Janu Chan chanj@bankofmelbourne.com.au (02) 8253 0898