Bendigo Bank

2022 Federal Budget Summary

As a follow up to last year's blockbuster 'pandemic budget', this year's Federal Budget was an excellent sequel. Last year's budget for FY21 was delayed until October for obvious reasons and set new records for spending and peacetime deficits; seven months on and the deficits are smaller, the outlook is immeasurably brighter, but the government's resolve to support the economy post-recession to a sustainable footing appears as firm as ever. The twist to the plot came via the size of the deficit for next financial year- over $106 bn, versus market expectations of around $80 bn, so the economic recovery should only gather pace from here, which will put pressure on higher interest rates over time.

The build up to this year's budget night left little doubt as to the government's focus - spending, incentives and targeted measures to lift employment and boost the economic recovery; and the details were entirely consistent with these aspirations.

Arguably the most contentious announcement was made a fortnight ago when Josh Frydenberg declared that 'budget repair' would not commence until the unemployment rate was closer to the RBA definition of full employment, so fiscal policy very much aligned to monetary policy. This explains why fiscal deficits fill the forward estimates- the table below shows the budget forecasts; and unless the unemployment rate falls below 4 ½ % in less than a year (which isn't completely out of the question) next year's budget will probably follow a similar path. However, with interest rates remaining at their record lows (the three-year bond yield is still at 0.1 %) the interest burden on this growing government debt is still falling as a share of GDP.

	2019-20 (actual)	2020-21 (estimates)	2021-22	2022-23	2023-24	2024-25
Underlying cash balance (bn)	-85.3	**-161.0**	**-106.6**	-99.3	-79.5	-57.0
% of GDP	-4.3	**-7.8**	**-5.0**	-4.6	-3.5	-2.4
Gross debt (bn)	684.3	**829.0**	**963.0**	1 058.0	1 134.0	1 199.0
% of GDP	34.5	**40.2**	**45.1**	48.6	49.7	50.0

Source: Budget Overview

Spending was broad based with few surprises, and (as well telegraphed in advance) concentrated on:

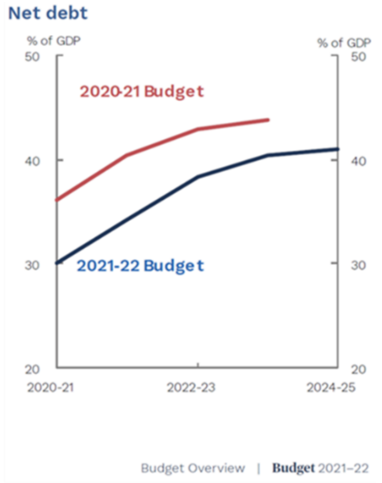
- Aged Care ($17.7 bn over five years)
- NDIS ($13.3 bn over four years)
- Health Care (including $2 bn for mental health)
- Child Care ($1.7 bn via an increased subsidy for second and subsequent children)
- Housing sector support
    - Family Home Guarantee (supporting single parents with as little as a 2% deposit)
    - New Home Guarantee (an extension of the First Home Loan Deposit Scheme)
    - First Home Super Saver scheme (increasing the maximum releasable amount to $50 000)
- Infrastructure investment ($15.2 bn over ten years)
- Tax relief (via an extension of the Low and Middle Income Tax Offset, worth $7.8 bn in 21/22)
- Business Investment, via the extension of the temporary full expensing for capex, and loss carry-back provisions.

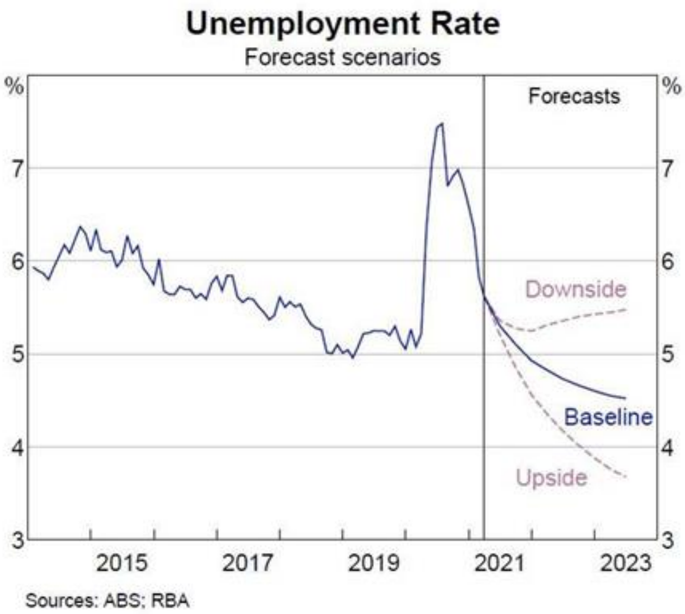
Areas open for criticism included insufficient allocation of spending on regional Australia, given the clear trend over the last year of demand for regional property and much higher levels of population growth outside the capital cities. The 'Building Better Regions' fund did receive $250 m in additional funding, and there were investments in water infrastructure (the $3.5 bn National Water Grid Fund) and digital infrastructure, but there could have been a greater emphasis on addressing skills gaps and regional job vacancies. Similarly, the lack of tourism specific measures has attracted criticism given the likely delays in reopening for international tourism (amid slow vaccination rates here), although domestic tourism is hoped to fill much of this gap. The budget also seemed to offer only cameo roles for green measures, with limited emphasis on renewables, and arguably was light on for affordable housing.

The debt profile has also come under close scrutiny, although the improved revenue side of the ledger (which may improve further given the conservative economic assumptions in the budget) means net debt has a much more benign profile, forecast to peak at just 40.9 % of GDP in 2025.

This profile is vastly superior to comparable economies around the world, on both a gross and net debt basis. As a result, the sovereign AAA credit rating remains intact, and while Standard & Poor's have the rating on negative outlook, they acknowledged the progress made, suggesting that fiscal support is driving the viability of the economic recovery.

The economic assumptions in the budget include GDP growing 4 ¼ % in 21/22, inflation remaining below 2% until 2023 and the unemployment rate to only fall to 5% in 21/22 and then to 4 ¾ % in 22/23. This is more conservative than the recently upgraded RBA forecasts (especially for unemployment as per below) and against the trend of recent jobs data, including very high levels of job vacancies and the fall in underemployment.





One of the reasons the fiscal position is so much stronger today than six months ago is the record high price for Iron Ore, currently above US$200 / tonne, but the budget has stubbornly retained a US$55 / tonne assumption. As a result, in the same way the budget position has greatly improved since October (despite the aggressive spending levels) we may well see sharp improvements to these budget deficits in the forward estimates, and hopefully a more rapid path to an unemployment rate below 4 ½ percent.

In summary, it was another big spending budget at a time when our economy does need this level of fiscal support arguably even more than it needs monetary policy support, given fiscal policy can be more targeted (as this budget is). The V-shaped recovery and elevated commodity prices mean the debt profile is quite manageable despite this level of spending, and while there may be some areas of the economy that didn't quite get their fair share, the aggregate impact will be positive. The economy still remains at the mercy of the pandemic (and needs an acceleration in the vaccine programme), but this budget will help with further jobs growth, business confidence and ultimately economic growth.

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