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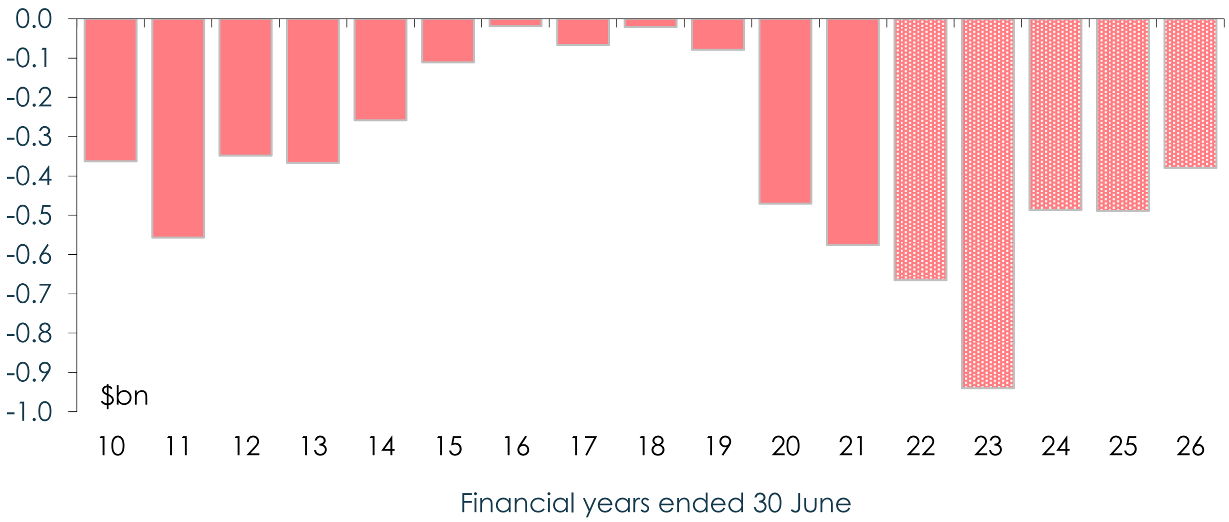
The 2022-23 Tasmanian State Budget: an 'instant' analysis

Treasurer Michael Ferguson's first Budget is a surprisingly big-spending affair, entailing new 'operating' spending (compared with what had been projected in last year's Budget) of $753mn over the four years to 2025-26, together with revenue reductions totalling $137 million over this period, plus an additional $236mn in new infrastructure and other 'capital' spending. As a result, and notwithstanding some 'windfall gains' from upwards revisions to forward estimates of revenue from state taxation and grants from the Commonwealth Government, the Government will be running larger underlying net 'operating' and cash deficits in each of the next three years, and net debt will be more than $1 billion higher in three years' time, than had been forecast in either last year's Budget or in February's Revised Estimates Report (RER).

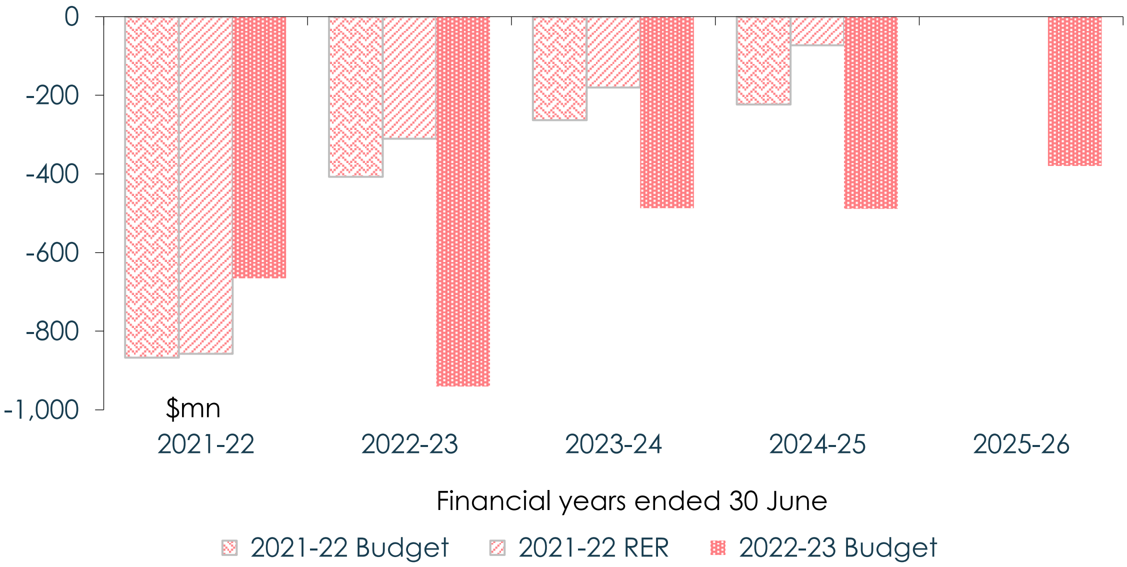
Formally, the Budget forecasts that the 'net operating balance' – that is, the difference between total revenue and 'operating expenses' (the costs of running government departments and agencies, plus grants and subsidies, interest expenses etc) which State Treasurers commonly use as 'the' measure of their 'bottom lines' will return to surplus in 2023-24, after incurring deficits of $456mn in 2021-22 (that's $233mn less than predicted in last year's Budget and $149mn less than in February's RER) and $475mn in 2022-23 (that's $388mn *worse* than predicted in last year's Budget, and $565mn worse than in the RER). The return to surplus on this measure has been put back by one year since February – the RER had projected a net operating surplus of $91mn in 2022-23. And the net operating surpluses projected for 2023-24 and 2024-25, of $19mn and $31mn respectively, are $173mn and $167mn smaller than forecast in February. Moreover, those projected operating surpluses owe more than they did in February, or in last year's Budget, to 'one-off' grants from the Commonwealth Government for capital, rather than operating, purposes.

The *underlying* net operating balance will remain in deficit throughout the forward estimates period – by $1.0bn more than had been forecast in last year's Budget, and by $1.35bn more than forecast in the RER over the three years to 2024-25, and by a further $410mn in 2025-26.

General government 'underlying' net operating balance ,2009-10 to 2025-26



Successive estimates of the 'underlying' net operating balance



The improvement in the 'underlying' net operating balance for the financial year that's about to end (2021-22) compared with the forecasts in last year's Budget and in February's RER is largely due to the additional $160mn which Tasmania will receive from the GST, and $316mn from other Commonwealth grants, compared with what had been projected a year ago.

The deterioration in the 'underlying' net operating balance forecast for 2022-23 through 2024-25 (shown in the second chart above) is largely due to the additional spending (totalling $753mn over these three years, by comparison with last year's Budget projections, or by $957mn over the four years to 2025-26) funded in this Budget, of which the largest components are $120mn (rising to $166mn when the 2025-26 financial year is included) for health, and $126mn ($151mn including 2025-26) for various State Growth projects.

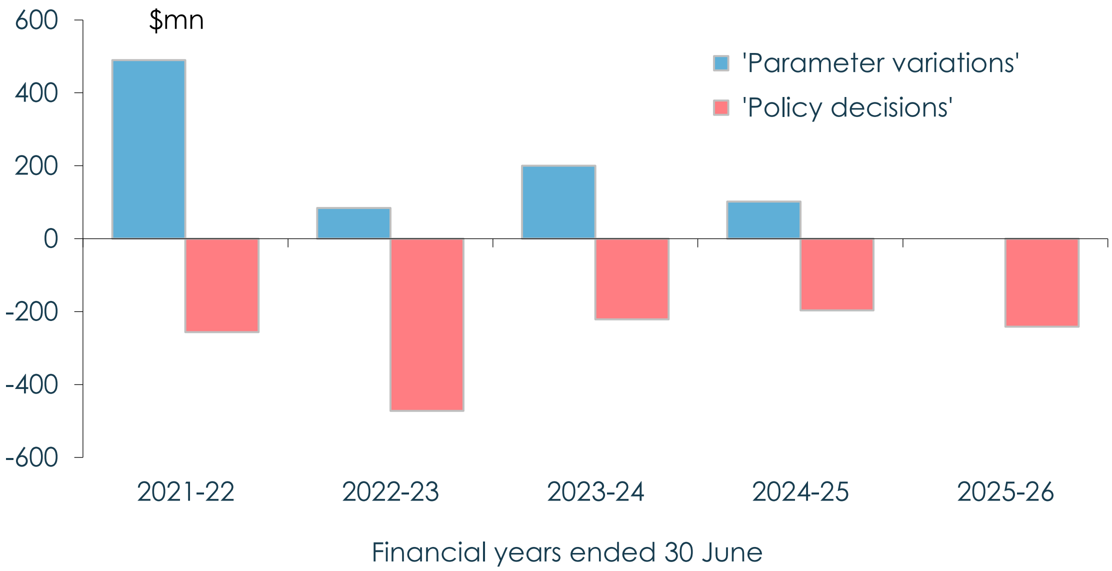
There's also an additional $100mn for the "Treasurer's Reserve Allocation" in 2022-23, which a footnote describes as being for "unexpected Covid-19 pandemic and other costs which could not be reasonably foreseen at the time of developing the 2022-23 Budget", and $180mn over the years 2023-24 through 2025-26 for "continuation of time limited programs" (which another footnote helpfully says "reflects funding to be allocated to agencies for the continuation of time limited programs over the forward estimates").

Another contributor to the forecast deterioration in the 'underlying' net operating balance are policy decisions to reduce revenues by $137mn over the three years to 2024-25 (or by $173mn over the four years to 2025-26), the bulk of which is the result of the reductions in land tax announced by former Premier and Treasurer Peter Gutwein earlier this year.

The 'bottom line' effects of these 'policy decisions' were partly offset by what the Budget Papers call 'parameter variations' – changes in estimates of revenue or spending which are the result of changes in underlying economic or other assumptions used in making forward estimates, including those relating to grants from the Commonwealth.

These boosted forecast revenues (compared with last year's Budget) by $1.24bn over the three years to 2024-25, mainly via upward revisions to forecasts of revenue from stamp duty, land tax, payroll tax and specific purpose grants from the Commonwealth, partly offset by upward revisions to forecast expenses (due, eg, to greater demand for spending in areas such as health).

Impact of 'policy decisions' and 'parameter variations' since last year's Budget on the net operating balance for 2021-22 through 2025-26

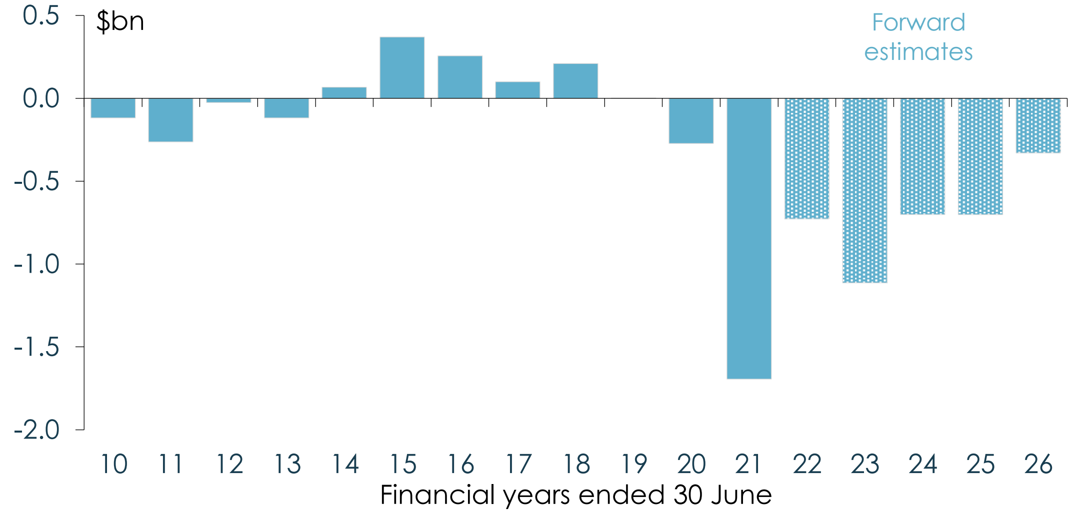


In addition to the additional 'operating' expense and revenue decisions, this year's Budget also includes new 'capital expenditure' policy decisions totalling $236mn over the three years to 2024-25 (or $304mn including 2025-26): while 'parameter variations' (presumably mostly due to cost escalations) have added $553mn to the estimated amount of infrastructure investment and other capital spending over the three years to 2024-25.

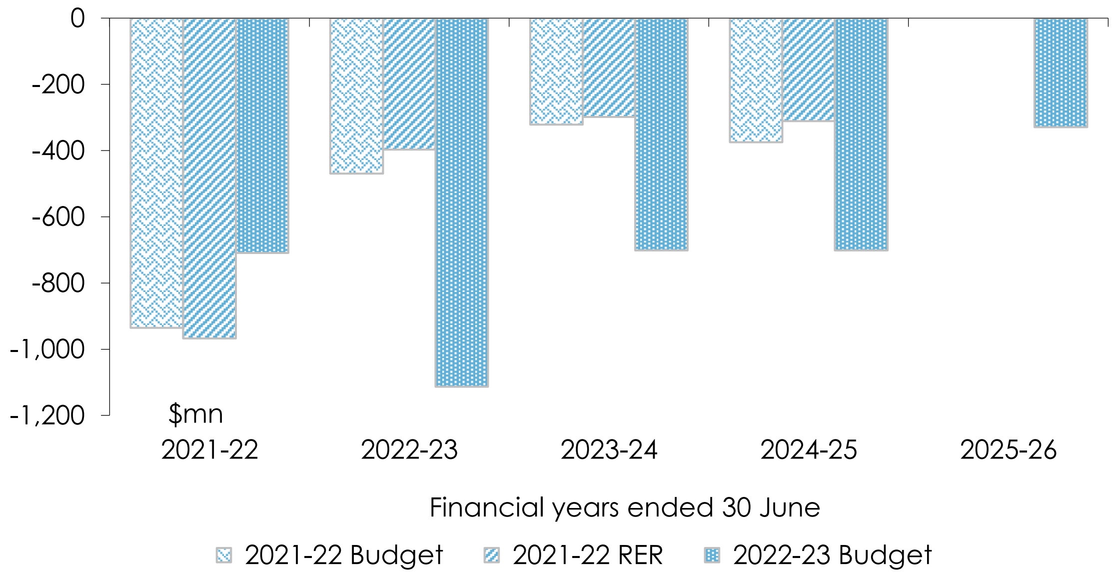
The net effect of the deterioration in the operating balance, and the increases in capital expenditures, since last year's Budget and the February RER is that the Government will be running larger *cash deficits* than previously forecast – a total of $2.5bn over the three years to 2024-25, $1.35bn more than projected for these three years in last year's Budget, and $1.5bn more than projected in the RER.

Add in the $329mn deficit forecast for 2025-26, and the Government will have incurred cash deficits totalling $4.3bn between 2019-20 (when the budget went into cash deficit for the first time since 2012-13) and 2025-26.

Tasmanian general government cash balance, 2009-10 to 2025-26



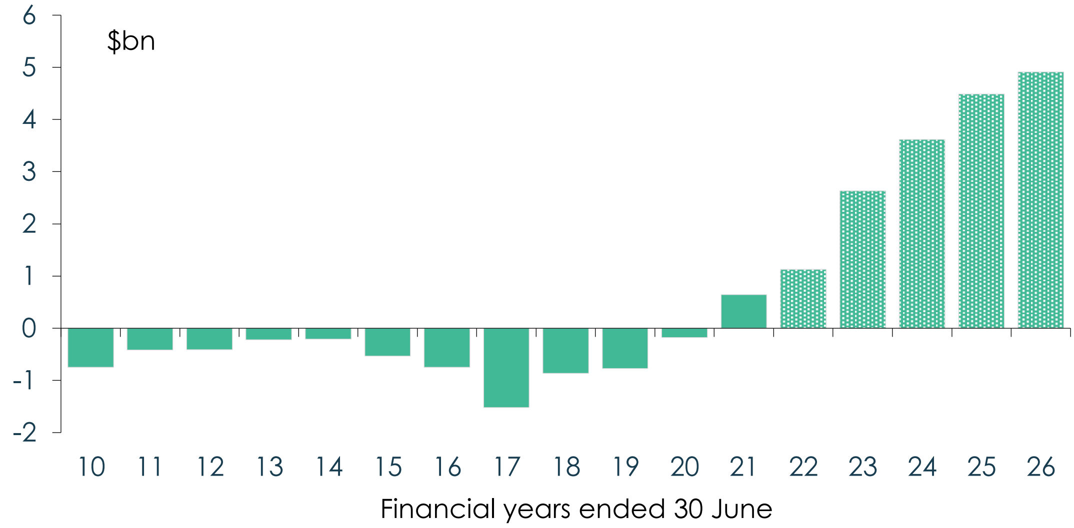
Successive estimates of the cash balance



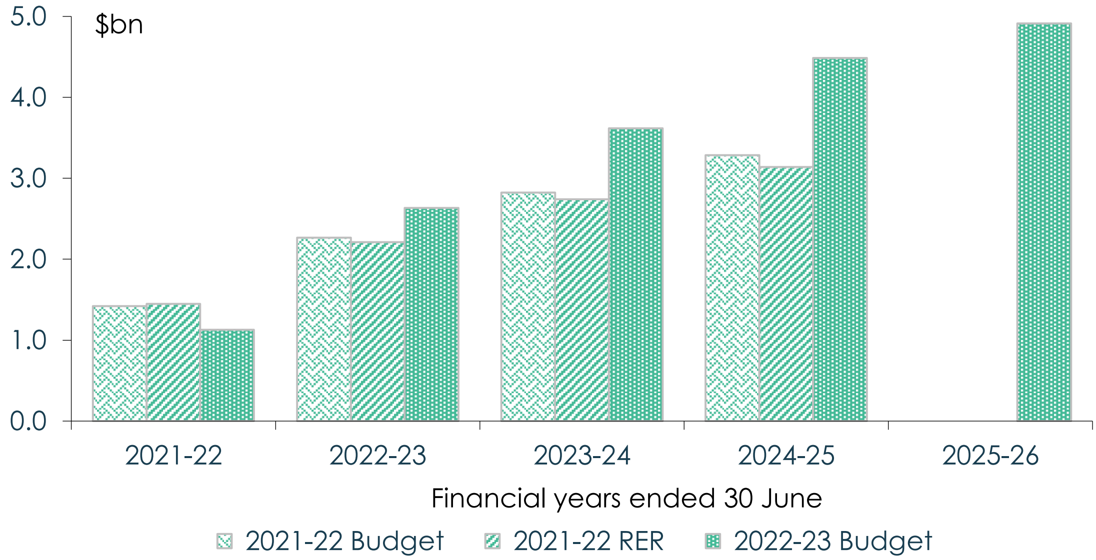
As a consequence of the larger cash deficits now being forecast, the Government's net debt (measured in accordance with Government Finance Statistics, or GFS, standards) will be significantly higher over the forward estimates period than previously forecast. 'General government' net debt is projected to reach $4.5bn by 30th June 2025, $1.2bn more than forecast in last year's Budget and $1.35bn more than forecast in February's RER, and to rise further to $4.9bn by 30th June 2026.

This latter figure is equivalent to about 11.3% of forecast gross state product, the highest this percentage has been since 1998-99.

Tasmanian general government net debt, 2009-10 to 2025-26



Successive estimates of net debt



Tasmania's total non-financial public sector net debt, ie including that of GBEs such as Hydro Tasmania and TasNetworks, is projected to rise from $3.8bn at 30th June this year (equivalent to just under 10% of GSP) to $10.2bn (equivalent to about 23¼% of forecast GDP) by 30th June 2026. This will likely be higher than for any other state or territory except Victoria and the Northern Territory.

One consequence of this increase in debt is that interest expense is expected to more than quadruple, from $47mn in 2021-22 to $206mn by 2025-26, or from 0.6% of total revenue in 2021-22 to 2.4% by 2025-26. This in turn means that the combined cost of debt service payments and defined benefit superannuation costs will reach 6.3% of cash receipts in 2025-26 – exceeding the Government's fiscal strategy limit of 6%.

In response, the Budget Papers state that “the Government will take action as required to achieve all the Strategic Actions over the medium term” and will “rebuild the fiscal buffers to provide the budget flexibility to respond to future shocks in a measured way over time, which does not impact on the provision of essential Government services”. There was no indication anywhere else in the Budget Papers as to what such ‘action’ might entail, or when it might be taken.

The Budget Papers were also surprisingly muted in their criticism of the changes to the GST revenue sharing arrangements imposed by the Morrison Government in 2018, and being ‘phased in’ between 2021-22 and 2026-27, which give Western Australia a much larger share of revenue from the GST than it would have been entitled to under the long-standing ‘horizontal fiscal equalization’ principles which had previously (going back to the 1930s) been used to determine the distribution of Federal ‘general purpose’ grants, and since 2000-01 the revenue from the GST, among the states and territories.

The other states and territories, including Tasmania, are temporarily protected from the otherwise inevitable reductions in their GST revenues by a ‘tra% nsitional guarantee’ that the Federal Government will ‘make good’ any shortfall between what they receive under these new arrangements and what they would have received under the previous system – which will require the Federal Government to add more than $20 billion to the deficits it will incur over this period in order to bolster Western Australia’s surpluses.

But that ‘transitional guarantee’ is set to expire at the end of 2026-27 – after which, unless it is extended, or the GST revenue sharing formulae reverts to its previous form, Tasmania in particular (given its greater reliance on its share of GST revenue than any other jurisdiction except the Northern Territory) stands to be considerably adversely affected.

In his Budget Speech, the Treasurer said, “as a small state we should not be losing out to other states that are swimming in mining royalties and posting multi-billion-dollar surpluses”. There’s only state which fits that description – and why the Treasurer didn’t name it explicitly, or go on to say any more than that it would be “a test for the new Federal Government and whether they will govern for all” isn’t clear.

Perhaps it was because it was his former Federal colleagues who imposed these new arrangements in what was ultimately a failed attempt to preserve their political position in Western Australia.

But it is indeed difficult to reconcile Federal Labor’s commitment to this ‘deal’ with its professed concerns for equity, or its post-election concerns about the urgency of ‘budget repair’.

The deterioration in the State Government’s budgetary position is surprising not only by way of contrast with its stated commitments to prudent financial management, but also in light of the positive[32] outlook for the Tasmanian economy presented by State Treasury in the Budget Papers.

Treasury is forecasting that Tasmania’s real gross state product will grow by 2¾% in 2022-23 and by 3% in 2023-24, after a strong 3¾% out-turn expected for 2021-22, before converging (by assumption) to the longer-term average of 2¼% per annum in 2024-25 and 2025-26.

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Conservatively, it expects employment growth to slow from 2¼% in 2021-22 to 1¼% in 2022-23 and to 1% pa thereafter, which allowing for a small increase in the labour force participation rate results in the unemployment rate rising from 3.8% most recently in April to 4½% in 2022-23 and remaining around that level for the following three years.

Properly, it notes "the ongoing evolution of the Covid-19 pandemic", the responses of consumers and businesses to prospective increases in interest rates, and "current and ongoing global political events" as risks to this outlook. But if those risks don't eventuate, or turn out to be relatively small in their impact on the Tasmanian economy, the Government's finances should be in better shape than this Budget forecasts.

In his short time in office, Premier Jeremy Rockliff has shown a greater willingness to make bold changes than his two Liberal predecessors – especially with yesterday's proposal to return Tasmania's House of Assembly to 35 members. He and Treasurer Ferguson will need to show a similar willingness to embrace bold ideas in their management of the budget over the remaining three years of the current Parliament if they wish to go to the electorate with a healthier set of fiscal numbers than those set out today.

(I thank the Treasurer and his office for giving me an embargoed copy of the Budget Papers earlier today which has allowed me to provide this commentary earlier than if I had had to wait until 3pm).

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