EUROPEAN UNION

DELEGATION TO AUSTRALIA

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AUSTRALIAN QUARTERLY ECONOMIC REPORT - DECEMBER 2012

KEY FIGURES FOR SEPTEMBER QUARTER 2012 (UNLESS OTHERWISE SPECIFIED)

GDP change	0.5% quarterly and 3.1% annually
Unemployment rate (Nov)	5.2%
Annual Inflation rate	2.0% headline and 2.6% underlying
Current account balance	-$A14.9bn; -4.0% of GDP
Terms of trade	-4.0% quarterly and -13.6% annually
Trade balance (Oct)	-$A2.1bn for goods and services
Exchange rate (at 30/11)	1 $A= €0.803; 1 $A=$US1.04; TWI=77.2
Cash interest rate (December)	3.0%
Budget balance (2012-13)	+$A1.1bn or 0.1% of GDP forecast

OVERVIEW

The Australian economy as measured by its **GDP** grew by 0.5% in the September 2012 quarter and by 3.1% annually, down from 3.8% in June. The main drivers for growth were business investment in machinery and equipment, changes in inventories and household expenditure on the expenditure side; and mining, manufacturing and health care and social assistance on the production side.

The **current account deficit** for the September quarter increased by 20% to -$A14.9bn or 4% of GDP. Australia's terms of trade fell by 4% in the September quarter and 14% annually, resulting in net national disposable income decreasing by 0.2% annually.

The **labour market** is showing signs of weakness, with employment growing by 1.1% annually. The participation rate in November eased to 65.1%, which allowed the unemployment rate to decrease to 5.2%.

The headline **inflation** rate for the September quarter was at 2.0% annually, although the Reserve Bank of Australia's (RBA's) preferred underlying inflation (weighted median) increased by 2.6% annually, within the RBA's target band of 2-3% over the cycle.

The RBA Board, at its meeting on 4 December, decided to ease **monetary policy** for the sixth time since October 2011 and cut the official interest rate to 3.0%. As a result monetary policy is clearly on an expansionary setting, unlike fiscal policy.

The updated **fiscal outlook** for 2012-13, including a range of budget saving measures, is for a wafer thin budget surplus of $A1.1bn (0.1% of GDP) and reflects the government's determination to achieve a budget surplus for political reasons. Net debt is expected to have peaked at 10% of GDP in 2011-12 and will decline to 9.4% of GDP in 2012-13.

Revised official **economic forecasts** expect the economy to grow at just under trend at 3% in 2012-13 and through to 2015-16 (*cf* 3¼% for 2012-13 in the Budget). Unemployment is expected to be at 5½% in both 2012-13 and 2013-14, declining to 5% in the outlook years. Headline and underlying inflation are forecast to remain in the bottom half of the RBA's target band, when the one-off impact of carbon pricing is excluded.

This quarterly report also contains a special section discussing Australia's monetary policy.

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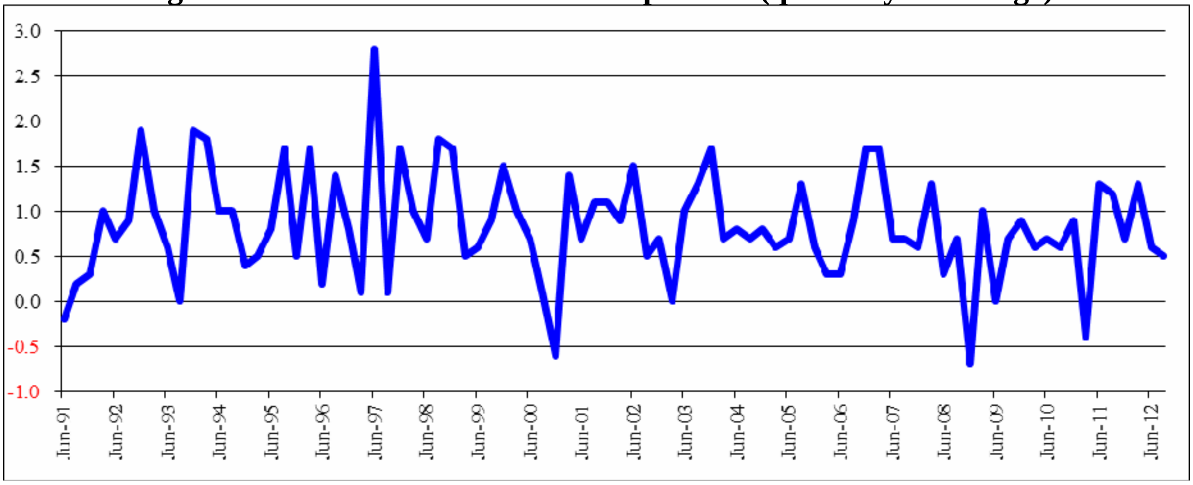
AUSTRALIAN ECONOMIC DATA UPDATE

National Accounts

According to the National Accounts (released on 5/12), **Gross Domestic Product** in seasonally adjusted[1] volume terms increased by 0.5% for the September quarter (see figure 1) which was just below market expectations (0.6%) and the slowest quarterly growth rate since March 2011. On an annual basis (quarter 2012 on quarter 2011) GDP growth of 3.1% was recorded for the September quarter, down from 3.8% recorded in the previous quarter and slightly below trend (3.4%). Treasurer Swan described the outcome as demonstrating *'the ongoing resilience of the Australian economy in the face of a difficult and volatile global environment.*'

Figure 1: Australian Gross domestic product (quarterly % change)



On the **expenditure** side, GDP for the September quarter was mainly driven by business investment in machinery and equipment (+6.2% quarterly, +1.6% annually and contributing +0.4 percentage points [ppts] to growth for the quarter) and in changes in inventories (+0.3ppts). Increases in household expenditure was also important (+0.3% quarterly, +3.3% annually and +0.2ppts to overall growth); with exports making a positive contribution (+0.8% quarterly, +4.7% annually and +0.2ppts) as did intellectual property products (+2.4% quarterly, +6.0% annually and +0.1ppts). Countering these were declines in public gross capital formation (-0.4ppts); a statistical discrepancy (-0.2ppts); and lower government consumption expenditure (-0.1ppts).

On the **production** side, there was a significant positive contribution from mining (+0.4ppts); while manufacturing, health care and social assistance and a statistical discrepancy all added 0.1ppts. On the other hand three sectors (agriculture, forestry and fishing; transport, postal and warehousing sectors; and professional, scientific and technical services) all subtracted 0.1ppts from growth for the quarter.

At a **state / territory level** domestic final demand grew by 0.2% for the quarter, by 3.7% annually and overall contributed 0.2ppts to growth. The only significant contribution to growth was made by the mining state of Western Australia (+2.3% for the quarter, 9.6% annually and +0.3ppts) with New South Wales having subdued growth (+0.1% for the quarter, 2.9% annually). All other states / territories subtracted from growth, led by Queensland (-1.6% for the quarter, +2.7% annually and -0.3ppts), South Australia (-3.2%, -0.1ppts) and the Northern Territory (-2.9%, -0.1ppts). Tasmania is firmly in recession (-2.0% quarterly and -5.7% annually), while the ACT has come off its highs (-0.8%, +5.6%) and Victoria is sluggish (-0.2%, +1.6%).

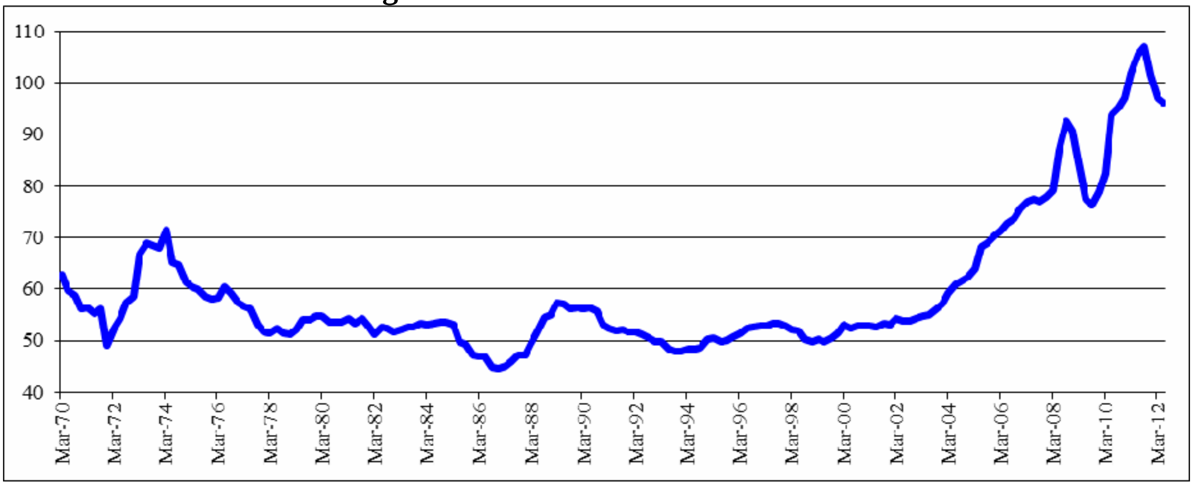
On the back of weakening iron ore, coal and other commodity prices, Australia's **terms of trade** (the relationship between prices and exports and imports) fell by a further 4% in the

[1] All indicators are in seasonally adjusted terms, unless otherwise indicated

September quarter and by 14% on September 2011 when they reached their highest point since records commenced in 1959. Nevertheless, the level is still 19% above the average for the last decade and over 56% above the average since 1959 (see figure 2).

As a result, real net national disposable income, a broader indicator of national economic well-being which includes both the volume measure of GDP and the terms of trade effect, fell by 0.7% for the quarter and fell by 0.2% annually compared with a growth of 3.1% for GDP.

Figure 2: Australia's terms of trade



Underlying the importance of population growth to Australia's economic growth, GDP per capita was flat (+0.0%) in the September quarter and grew by only 1.4% annually.

Productivity, as measured in GDP per hour worked, increased by 0.8% for the September quarter and by 3.3% year-on-year (compared to an average annual increase since 1978 of 1.6%).

Demand

Retail sales (7/12) for October were flat (0.0%) in current price terms, to be 3.1% higher annually. For the September quarter retail sales were also flat (-0.1%) on the June quarter in volume terms and increased by 3.2% year-on-year.

New motor vehicle sales (15/11) in October decreased by 2.8% for the month to be still a strong 8.6% higher annually. Industry estimates (5/12) point to strong sales for November (+10.9% and +9.8% year to date) and with sales already in excess of one million for 2012, record car sales are expected for the full year of around 1.1 million.

Forward indicators for the housing sector are mixed and remain subdued compared to longer-term levels. Total building approvals (4/12) decreased by 7.6% in October to be 14.5% higher annually; while the value of housing finance (12/11) was 3.5% higher in September and 5.9% higher annually.

The index of established average house prices (6/11) increased in the September quarter by 0.3%, with increases in 5 of the 8 capital cities, to be just 0.3% higher on an annual basis. The HIA housing affordability index (27/11) rose for the seventh consecutive quarter in the September quarter by 5.3% to be 15% higher than a year earlier.

The September **quarter** 2012 headline inflation (24/10) increased by a higher than expected 1.4% for the quarter and by 2.0% annually (up from 1.2% in the June quarter); while the Reserve Bank of Australia's (RBA's) preferred underlying inflation (weighted median) increased by 2.6% annually, within the RBA's target band of 2-3% over the cycle. The quarterly increase in headline CPI includes the impact of the carbon price introduced on 1 July 2012, with the Treasury estimating that it would lead to a one-off 0.7% increase consumer prices in 2012-13. Producer Price Indexes (2/11) for the September quarter were on the softer side with the final stage prices increasing by 0.6% for the quarter and 1.1% annually, suggesting limited upstream inflationary pressures in the short term.

Overall private sector credit (30/11) growth continues to be moderate, with credit increasing by just 0.1% in October and by 3.8% annually. Housing finance rose annually by 4.7% and business finance by 3.3%, while personal finance declined by 0.3% year-on-year.

Business conditions

Sales (3/12) of goods and services were higher at both manufacturing and wholesale levels by 1.3% and 2.0% respectively for the September quarter, to be 2.2% lower annually for manufacturing sales and 6.3% higher for the wholesale sales.

Inventories (3/12) for the September quarter increased by a stronger than expected 1.1% quarterly, to be 4.0% higher on an annual basis.

Gross operating company profits (3/12) fell by 2.9% quarterly in line with expectations, to be 13% lower on an annual basis.

Private new capital expenditure (29/11) increased broadly in line with expectations by 2.8% in volume terms for the September quarter to be 14% higher than a year earlier. Within this, buildings and structures were up 20% annually and equipment, plant and machinery up by 5%. The outlook for the current year points to the investment surge continuing, with expected new capital expenditure for 2012-13 (fourth estimate) at $A173bn, some 5% higher than the comparable estimate for 2011-12, but not as strong a previously expected being 3% lower than the third estimate recorded last quarter.

Labour Market

To the surprise of the market, which expected no change, employment (6/12) increased by 13,900 persons (full-time employment decreased 4,200 persons while part-time employment increased 18,100 persons) to 11.5mn in November, with year-on-year employment growing by 1.1%. The **participation rate** eased by 0.1ppts to 65.1%, resulting in the **unemployment rate** falling by 0.1ppts to 5.2% (see figure 5).

Figure 3: Australia's unemployment rate (%)

The ANZ overall job advertisements index (3/12) provides a leading indicator of employment (~6 months), with the aggregate index falling for the eighth consecutive month in November by 2.9% (newspaper advertisements -4.6%, internet job advertisements -2.8%) to be 17% lower year-on-year. The ANZ concludes that *'without a solid pick-up in the non-mining sectors … the unemployment rate is set to drift higher to 5.75% by mid-2013'.*

On labour costs, the Wage Cost Index (14/11) increased in trend terms by 0.9% in the September quarter to be 3.7% higher than a year earlier. The average annualised wage increase for federal enterprise bargaining increased by 3.6% for the September quarter.

External Transactions

The balance of payments (4/12) current account deficit for the September quarter increased by 20% from -$A12.4bn to -$A14.9bn (estimated 4.0% of GDP). This was due to a decline in the terms of trade which in turn led to a 120% or $A2.5bn increase in the deficit on trade in goods and services to -$A4.6bn. The net primary income deficit was unchanged at -$A10.0bn. In volume terms, exports increased by 0.8% while imports increased by 0.1% for the quarter to be 4.7% and 3.5% higher annually.

Arguably a structural weakness in the Australian economy is the size of its **net foreign debt.** For the September quarter, Australia's net foreign debt was flat (-0.3%) on the June quarter level to total $A749bn which is 2% higher year-on-year. This represents around 55% of Australia's annual GDP. Over 70% of this debt is in the private sector. The net interest cost on the debt for the September quarter was $A5.0bn or 1.5% of quarterly GDP.

The subsequent monthly statistics for October (7/12) show a deficit in the balance of goods and services of $A2.1bn (up by $A0.7bn or 47% on September's $A1.4bn deficit). This was mainly due to imports increasing by 3% to $A26.5bn, while exports were only marginally higher at $A24.4bn.

On a year-to-date basis (January-October) Australia's merchandise exports have fallen by 3.7% to $A207.6bn. China remains Australia's major export destination this year (29% of all exports), although recent monthly data is slightly down from a year earlier. The EU is Australia's fourth largest export market (7%). Australian imports are up 8.3% to date in 2012, to $A201.0bn, with the EU (7.7%) having been recently been supplanted by China (18.1%) as Australia's largest supplier of goods - see Table 1.

Table 1: Australia's trade in goods by major partners (year to date)

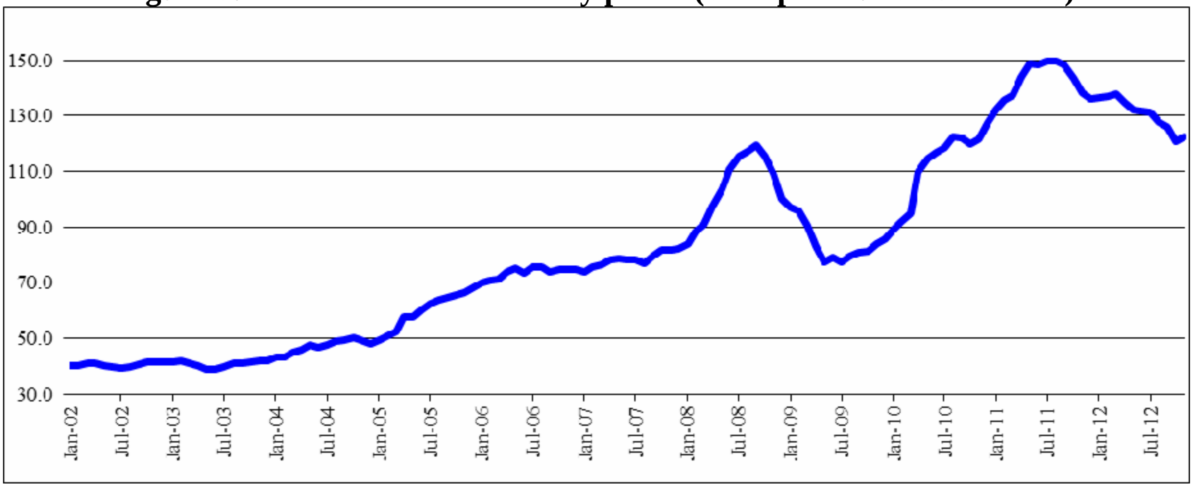
	January to October ($Amn)			Share of total %			% change
	2010	2011	2012	2010	2011	2012	2012/11
Exports							
China	46,771	58,805	60,689	24.6	27.3	29.2	3.2
Japan	35,875	41,266	40,541	18.9	19.1	19.5	-1.8
Korea	16,613	18,961	16,799	8.7	8.8	8.1	-11.4
EU	15,602	15,209	14,193	8.2	7.1	6.8	-6.7
Total	*190,194*	*215,511*	*207,568*				*-3.7*
Imports							
China	31,722	34,202	36,281	18.4	18.4	18.1	6.1
EU	31,950	33,309	35,642	18.5	18.0	17.7	7.0
United States	18,790	20,720	23,370	10.9	11.2	11.6	12.8
Japan	15,150	14,610	15,949	8.8	7.9	7.9	9.2
Total	*172,792*	*185,554*	*200,955*				*8.3*

The Australian dollar has been very strong for most of the year and on a trade-weighted basis at the end of November (77.2) had eased by 3% since the 27-year peak on 02/03/12 of 79.3 (see figure 6). Vis-à-vis the euro, the $A has been particularly strong and was at 1$A=€0.8025 at the end of November which was 6% lower than the all-time peak on 13/08/12. Against the $US, the $A has been above parity for most of the year and at the end of November was at $A1=$US1.04, some 6% below the recent nearly 30-year high (28/07/11 of $A1=$US1.106).

Figure 4: Movements in Australian dollar - Trade Weighted Index (end month)

Looking ahead, commodity prices as recorded by the RBA (3/12) have increased by 1.5% in November in SDR terms after falling by 2.9% in October (revised) and by 11.6% over the past year (see figure 5), suggesting an uncertain outcome in terms of trade in the December quarter.

Figure 5: RBA index of commodity prices (SDR prices: 2008/09 = 100)



OUTLOOK

Numerous forecasts have been released during the past quarter with some downward revisions in the outlook compared to earlier forecasts but still with a relatively healthy expectations for economic growth.

The first of the forecasts released was the IMF World Economic Outlook (9/10) which *'reaffirmed the strength of Australia's economic fundamentals in the face of a weaker global recovery, with the Australian economy again forecast to outperform every major advanced economy over this year and next'*. The IMF upgraded its forecast for Australia for 2012 from 3.0% to 3.3% and downgrading the 2013 forecast from 3.5% to 3.0%. The updated data ranks the Australian economy as the 12th largest in the world.

Secondly, the **official government** MYEFO estimates (22/10) were presented within the context of downgraded global growth forecasts, with risks to the international growth outlook remaining firmly on the downside – notably the threat of financial contagion from the crisis in the euro area and the potential fiscal cliff in the United States threatening an already fragile recovery. These risks and uncertainties in the international outlook are expected to persist into 2013.

Nevertheless, the Australian economy is expected to grow at around trend 3% in 2012-13 and through to 2015-16 (*cf* 3¼% for 2012-13 in the Budget), which the MYEFO states is 'faster than every major advanced economy' (see Table 2).

This growth continues to be underpinned by a surge of investment in the resources sector (business investment +11% in 2012-13 and +6½% in 2013-14); strong growth in the volume of commodity exports (+4.5% in 2012-13 and +4% in 2013-14); and solid household demand (+3% in both 2012-13 and 2013-14).

Table 2 Major economic parameters[(a)]

	Forecasts		Projections	
	2012-13	2013-14	2014-15	2015-16
Real GDP	3	3	3	3
Employment	1	1 ¼	1 ½	1 ½
Unemployment rate	5 ½	5 ½	5	5
Consumer Price Index	3	2 ¼	2 ½	2 ½
Nominal GDP	4	5 ½	5 ¼	5 ¼

(a) Real and nominal GDP are year-average growth. Employment and CPI are through-the-year growth to the June quarter. The unemployment rate is the rate for the June quarter.
Source: Treasury.

Unemployment is expected to be at 5½% in both 2012-13 and 2013-14, declining to 5% in the outlook years. The MYEFO highlights that this is 'in stark contrast to the high unemployment rates in major advanced economies'. Headline and underlying inflation are forecast to remain in the bottom half of the RBA's target band (2-3%), when the one-off impact of carbon pricing is excluded.

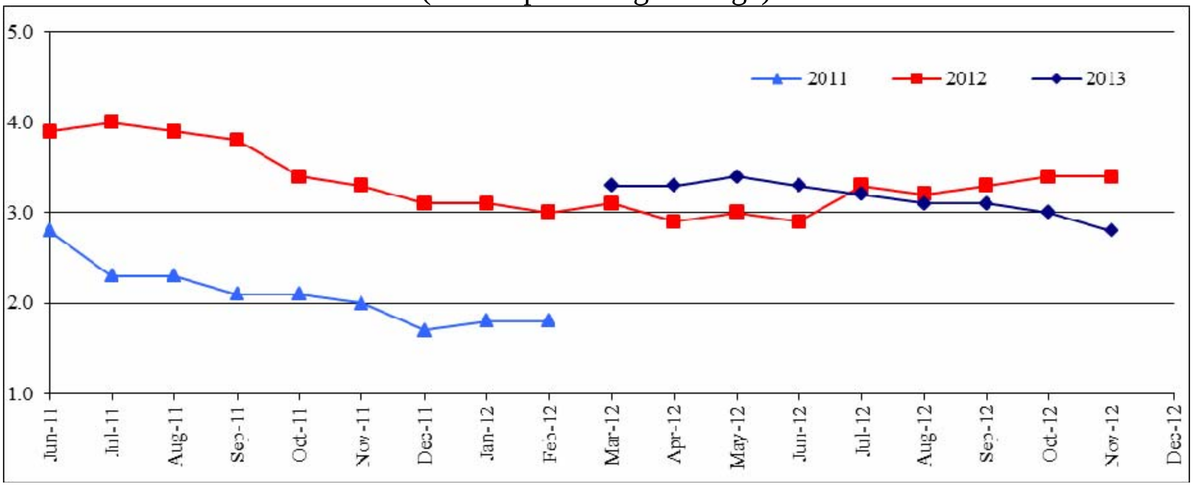
The larger anticipated slowdown in China and the impact this has had for global commodities markets and Australian export revenues is highlighted as a key challenge for Australia. In this respect, Australia's terms of trade is now forecast to decline by 8% in 2012-13 (*cf* -5¾%), resulting in nominal GDP expected to grow by 4% for 2012-13 (*cf* 5½%) which is adversely impacting on tax receipts. There is considerable uncertainty whether the new forecasts are still too optimistic and further falls in the terms of trade would adversely impact on nominal growth and the fiscal situation.[2]

Thirdly, the **RBA** issued its revised forecasts in its quarterly statement on monetary policy (9/11). It expects growth to be at 3.5% year ending December 2012 (unchanged on August). For the outlook period the RBA eased down its forecasts since August to just below trend with growth, with GDP growth expected to be a little below 2¾% during 2013 before picking up to just under 3% over 2014. The downward revision reflects lower expected mining investment, which reduces expected growth by ½%. The RBA's outlook for inflation is largely unchanged, with the introduction of the carbon price expected to increase inflation to over 3% in the near term, falling back to around the middle of the target range (2-3%) in a year's time.

Fourthly, ***The Economist*** November poll of GDP forecasts (10/11 – see figure 6) puts Australia’s rate of growth amongst the fastest for the major developed economies covered for 2012. The poll suggests expected GDP growth for Australia in 2012 will be at 3.4% (unchanged in November with a range from 2.1% to 4.0%) and 2.8% for 2013 (revised down from 3.0%, range 2.1% to 3.5%). Inflation is expected at 1.8% for 2012 (down from 1.9%), increasing to 2.7% for 2013 (unchanged). The current account deficit as a percentage of GDP is now expected to be at -3.7% in 2012 (up from -3.6%) and at -4.5% in 2013 (up from -4.3%).

[2] Sensitivity analysis in MYEFO suggests that a 1% decrease in nominal GDP due to a 4% fall in the terms of trade would reduce receipts and the underlying cash balance by $A2.8bn in 2012-13 and by $A6.7bn in 2013-14.

Figure 6: Evolution of *The Economist* poll of GDP forecasts
(annual percentage change)



Fifthly, the OECD in its November Economic Outlook (27/11) forecast growth in Australia at 3.7% for 2012 (up from 3.1% in May forecast), 3.0% in 2013 (down from 3.7%) and 3.2% in 2014. The 2013 outlook compares with the OECD average of 1.4% growth. The OECD summarised the outlook as:

'Output is projected to expand by roughly 3¼ per cent in 2013 and 2014, which would be slightly below potential. Despite the decrease in the terms of trade, the mining sector can still be expected to sustain growth which remains marked by substantial sectoral disparities. Nevertheless, the high exchange rate, continued household deleveraging and budget-tightening in 2012/13 should damp activity in many other sectors.

In the absence of inflationary pressures, the current easing of monetary policy to stimulate demand is welcome. If the economic situation were to deteriorate significantly, the authorities should let the automatic stabilisers work and should slow budget consolidation. Sustaining a robust rise in the standard of living will entail bolstering productivity by pursuing reforms in taxation, infrastructure and innovation'.

MONETARY POLICY

The Board of the Reserve Bank of Australia announced after its December meeting (4/12) that it had decided to cut the cash rate by a further 25 basis points to 3.0%. This is the sixth easing since October 2011, with monetary policy now clearly on an expansionary setting, unlike fiscal policy. The cash rate is now at the same level as the lowest rate during the global financial crisis (April – September 2009). However, because not all the recent cuts have been passed on to consumers, the average variable mortgage rate is expected to be at least 0.6% higher than was applicable during the crisis (see figure 8, overleaf). As a result the impact of monetary policy easing has been muted (see the special section on Australia's monetary policy, overleaf).

In making the announcement the RBA concluded: *Over the past year, monetary policy has become more accommodative. There are signs of easier conditions starting to have some of the expected effects, though the exchange rate remains higher than might have been expected, given the observed decline in export prices and the weaker global outlook. While the full effects of earlier measures are yet to be observed, the Board judged at today's meeting that a further easing in the stance of monetary policy was appropriate now. This will help to foster sustainable growth in demand and inflation outcomes consistent with the target over time.*

AUSTRALIA'S MONETARY POLICY SETTINGS

Australia's monetary policy is determined by the Reserve Bank of Australia (RBA), a statutory authority established under the *Reserve Bank Act 1959*, which is also responsible for financial supervisory and central banking functions. The obligations of the RBA with respect to monetary policy are set out in the Act, namely the stability of the currency in Australia; the maintenance of full employment in Australia; and the economic prosperity and welfare of the people of Australia.

Policy framework and implementation

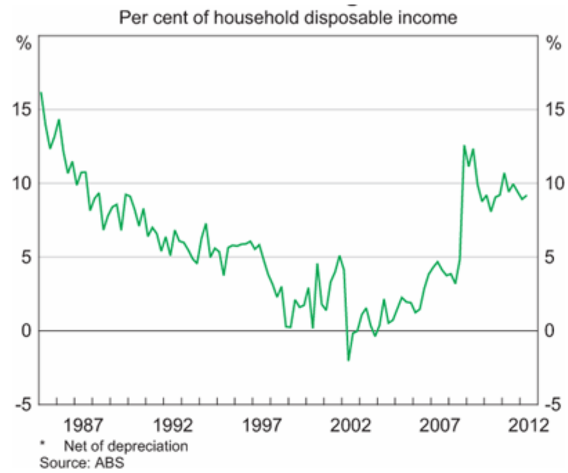
The framework for Australia's monetary policy is formalised in the *Statement on the Conduct of Monetary Policy* jointly issued by the Treasurer and the RBA Governor, and most recently revised in September 2010. It outlines the RBA's task of focusing on price stability and the implications for economic activity and employment, and specifies its objective of keeping inflation between 2-3%, on average over the medium-term, a target first adopted in 1993.

Monetary policy is decided upon by the RBA Board, which meets on the first Tuesday of each month, except in January, to set the operating target for the cash rate. The decision is made independently of the Australian Government, although the RBA is required under legislation to regularly inform both the Government and Parliament of the conduct of its monetary policy.

The current economic context

The Australian economy has in recent years experienced a period of significant structural change, brought about by a resurgent mining sector and terms of trade and investment boom. Combined with the destabilising effects of the global financial crisis, the oft-quoted "patchwork economy" emerged, bringing with it a raft of implications for the setting and transmission of monetary policy, such as the cautious consumer (see Figure 7), mixed levels of business confidence, changing bank funding costs and a persistently strong exchange rate. More recently, both the RBA and Government have had to confront the approaching peak of the mining investment boom and the implications this poses for future policy settings. Through all of this, the RBA has maintained that monetary policy's role is to keep inflation low and stable, "*so that difficult decisions at the firm and industry level are not further complicated by macroeconomic instability*", according to RBA Deputy Governor Phillip Lowe earlier this year.

Figure 7: Household Saving Ratio



An increasingly accommodative stance

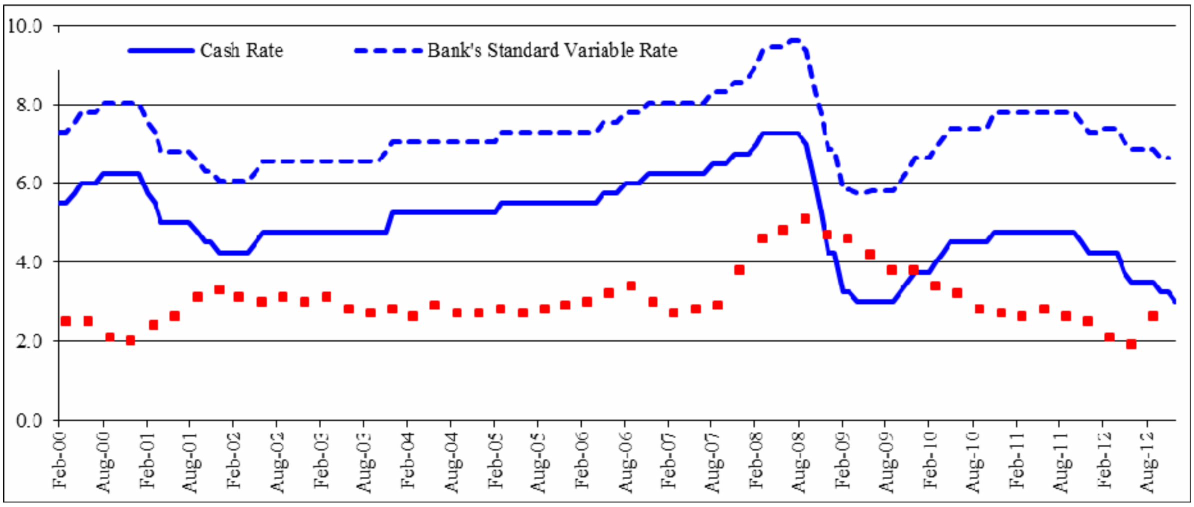
The RBA acted decisively with the onset of the global financial crisis, progressively lowering the cash rate from 7.25% in August 2008 to 3% by April 2009 in an attempt to underpin the Australian economy in conjunction with the Government's concerted fiscal expansion. As the economy showed signs of recovery, monetary policy was shifted back to a more neutral stance, with the cash rate remaining unchanged at 4.75% from December 2010 until October 2011. However, amidst sustained global uncertainties and a slightly more subdued domestic outlook, a renewed easing in monetary policy has been deemed necessary (encouraged in part by the Government's "*strong budget management*" in the words of the Treasurer), resulting in the cash rate being lowered to what the RBA terms an "accommodative" 3% as of December 2012.

Risks and uncertainties

The outlook for inflation appears relatively benign over the medium-term; the RBA forecasting in November that underlying inflation will remain within its preferred band of 2-3% through until the end of 2014. Although this provides the RBA with some flexibility in its responses, monetary policy in Australia still faces various challenges in a multi-speed economy, amongst which are questions over its present effectiveness to foster growth as the Government continues to pursue its policy of fiscal rectitude. Meanwhile, the RBA has signalled concern over the potential contractionary effect of the high exchange rate, and its impact on the non-mining sectors of the economy (leading some to speculate that it could intervene in foreign exchange markets).

In his much-publicised "glass half-full" speech on 8 June 2012, RBA Governor Glenn Stevens also acknowledged the limitations of monetary policy in dealing with the structural changes presently impacting the Australian economy, calling for a lifting of productivity, without which inflationary pressures could resurface.

Figure 8: Australia's official interest rates and underlying inflation rates (%)



FISCAL POLICY

The updated fiscal position (22/10) contained in the Mid-Year Economic and Fiscal Outlook (MYEFO) showed that since the Budget there has been a write-down in total tax receipts over the outlook period of around $A20bn (of which $A4bn are in 2012-13). With the Government committed to return the budget to a surplus in 2012-13 (July-June), it announced savings totalling $A16.4bn ($A2.1bn in 2012-13) and allowing for the $A6.1bn ($A716mn in 2012-13) impact of all policy decisions announced since the Budget, the net saving is $A10.5bn over the outlook period ($A1.4bn in 2012-13).

Savings / additional revenue have been achieved through a range of measures including reforms to improve the operation and integrity of the taxation and superannuation systems, notably a phased introduction of monthly pay-as-you-go instalments for large companies ($A8.3bn over 4 years) and greater compliance activities by the Australian Tax office ($A1.5bn); cuts to education and skills training ($A1.6bn); reforms to Private Health Insurance ($A1.1bn); increases in visa charges ($A520mn); and cuts to the baby bonus ($A506mn).

Among the new expenditure decisions announced since the Budget and included in the MYEFO are the funding of the Dental Health Reform package ($A4bn over 6 years); the response to the report of the expert panel on asylum seekers ($A497mn over 4 years); additional funding for the Tasmanian health system ($A325mn over 4 years); and funding for the Afghan National Security Forces ($A154mn over 2 years).

The underlying cash balance (the government's preferred measure) for 2012-13 is now expected to be a wafer thin surplus of $A1.1bn (*cf* $A1.5bn in the Budget) or 0.1% of GDP. This is expected to progressively increase to $A6.4bn in 2015-16 (*cf* $A7.5bn) or 0.4% of GDP. In accrual terms, a fiscal surplus of $A1.2bn (*cf* $A2.5bn) or 0.1% of GDP is estimated for 2012-13 (see table 3, overleaf).

Revenue in 2012-13 is now forecast to total $A373.7bn (*cf* $A376.1bn) or 24.4% of GDP rising to 24.9% of GDP by 2015-16. Expenses are expected to reach $A375.0bn (*cf* $A376.3bn) or 24.5% of GDP in 2012-13, rising to 24.7% in 2013-14 before easing back again to 24.3%.

Government net debt remains low by international standards, and is forecast to be at $A144.0bn (9.4% of GDP) in 2012-13, having peaked at 10% of GDP in 2011-12 and is expected to reduce to 7.7% of GDP by 2015-16.

Net financial worth (total financial assets minus total liabilities) is expected to be -$A257.9bn in 2012-13 or -16.9% of GDP (*cf* 16.0% of GDP) and to progressively improve to -13.0% of GDP by 2015-16.

Table 3 Budget aggregates

	Estimates			
	2012-13		2013-14	
	Budget	MYEFO	Budget	MYEFO
Underlying cash balance($bn)(a)	1.5	1.1	2.0	2.2
Per cent of GDP	0.1	0.1	0.1	0.1
Fiscal balance($b)	2.5	1.2	2.6	4.3
Per cent of GDP	0.2	0.1	0.2	0.3
	Projections			
	2014-15		2015-16	
	Budget	MYEFO	Budget	MYEFO
Underlying cash balance($bn)(a)	5.3	3.3	7.5	6.4
Per cent of GDP	0.3	0.2	0.4	0.4
Fiscal balance($b)	7.0	6.9	9.5	9.8
Per cent of GDP	0.4	0.4	0.5	0.5

(a) MYEFO figures report net Future Fund earnings, whereas Budget figures report gross Future Fund earnings.

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