

1.3 STATEMENT OF ECONOMIC AND OTHER ASSUMPTIONS

This statement of economic and other assumptions is made in line with section 11(1)(b) of the *Financial Management Act 1996*.

Economic Assumptions

The economic forecasts underpinning the 2005-06 Budget are summarised below.

Economic Forecasts						
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
	(Actual)	(Forecast)	(Forecast)	(Forecast)	(Forecast)	(Planning)
	(Average annual growth)					
	Percentage change on previous year ^a					
Gross State Product	1.5	2.0	1.8	1.5	2.3	2.5
Gross Domestic Product ^b	3.8	3.0	3.25	3.5	3.5	3.5 ^c
Employment Growth	0.0	1.5	1.0	1.0	1.5	1.5
Consumer Price Index ^b	2.9	2.25	2.25	2.5	2.5	2.5 ^c
State Final Demand	3.8	3.5	3.3	3.0	3.8	4.1
Interest Rates ^d	5.06	5.35	5.75	5.75	5.75	5.75
Population ^e	0.2	0.5	0.8	0.8	0.8	0.7

(a) Based on seasonally adjusted and original data currently available, with financial data expressed in real terms. Percentage changes are expressed in year average or year total terms unless otherwise indicated.

(b) Australian Treasury estimates included in the Mid-Year Economic and Fiscal Outlook, December 2004.

(c) ACT Treasury planning assumption.

(d) Reserve Bank of Australia, average annual cash rate target. The cash rate is the rate charged on overnight loans between financial intermediaries. It has a powerful influence on other interest rates and forms the base on which the structure of interest rates in the economy is built.

(e) As at 30 June each year.

State Final Demand (SFD) for 2004-05 is now expected to grow by 3.5% - higher than the 2.9% forecast in the Pre-Election Budget Update 2004-05 and higher than the 2.6% forecast at Budget. The higher forecast for 2004-05 is primarily driven by higher than expected growth in both household consumption and Commonwealth Government consumption, while private investment is expected to return to positive (albeit small) growth.

Private consumption is now likely to grow at around 3.3%, slightly higher than the 3.0% forecast underlying the 2004-05 Budget. The revised outlook is based on continued strength in the labour market flowing through to an increase in household incomes and solid growth in non-discretionary expenditure.

The 4.6% forecast for real Commonwealth outlays nationally in the 2004-05 Mid-Year Economic and Fiscal Outlook is up 1.0 percentage point on the 3.6% forecast contained in last year's Federal Budget. While an increase in Commonwealth outlays nationally will tend to increase economic activity in the ACT (e.g., public administration activity), the rate of growth in Commonwealth expenditure in the ACT has fallen below the national average in recent years. With the current expenditure priorities of the Commonwealth Government weighted towards regions other than the ACT, this trend is likely to continue.

Private investment is expected to rebound from the 5.0% fall recorded in 2003-04 to positive growth in 2004-05. The expectation of a return to positive private investment growth is consistent with The Sensis® *Business Index* for February 2005 that shows a net balance of 73% of ACT small to medium businesses are confident about business prospects over the next 12 months. Overall, total private investment remains at close to historic record levels.

Looking forward, growth in SFD is forecast to ease slightly to 3.3% as the real rate of growth of Commonwealth Government outlays falls from 4.6% in 2004-05 to 2.4% in 2005-06. Mitigating the easing in Commonwealth outlays, household consumption in the ACT is expected to remain strong.

Gross State Product (GSP) is forecast to grow by 2.0% in 2004-05, down on the Pre-Election estimate of 3.0%. The downgraded forecast for ACT GSP growth reflects an ongoing change in the relationship between production and demand in the ACT. For some time now, production in the ACT (as measured by GSP) has tended to represent a progressively smaller proportion of demand in the ACT economy (as measured by SFD). The nature of industry in the ACT (mainly white-collar) results in a high and increasing reliance on imports of goods and services for both intermediate use and final consumption.

The ACT labour market remains very strong, despite flat employment growth in the first part of 2004-05. The employment forecast for 2004-05 was revised down from 1.0% in last year's Budget to 0.75% for the Pre-Election Budget Update 2004-05.

The monthly labour force estimates show that the ACT began 2005 with the highest monthly gain in employment, in seasonally adjusted terms, since July 1987 - 2.9% in January 2005. While month-to-month movements in ACT labour force estimates are extremely volatile, based on employment data to March 2005 the year-average employment growth forecast for 2004-05 has been revised up to 1.5%.

The recent employment growth has mainly been supported by an increase in the labour force participation rate to near record levels. The employment forecasts for 2005-06 and 2006-07 are constrained to 1.0% growth by the expected continuation of the tight labour market nationally, an expectation that ACT labour force participation rates will plateau and a forecast slow-down in the rate of growth in real Commonwealth outlays.

Price movements in Canberra closely follow national trends. The national outlook for inflation is benign, with a rate of 2.25% forecast for both 2004-05 and 2005-06. The inflation forecast for the out-years is 2.5%, i.e., the mid-point of the Reserve Bank of Australia's target range of 2% to 3%.

Further detail on the Territory's economic conditions is available in Chapter 4.1.

Other Assumptions

Employee Wage Negotiations

Public sector wages growth can have a material impact on Budget estimates. Salary and wages consist of approximately 35% of 2005-06 expenses.

The Budget and forward estimates reflect the cost of wages for those employment categories where negotiations have been finalised. These include clerical, firefighters, teachers, nurses, an interim offer to Medical Officers and the re-classification of Health Professionals.

An expenditure provision has been made for planning purposes where negotiations are not materially progressed, and for future wage negotiations in the forward estimates beyond the terms of current agreements.

Treasurer's Advance

The forward year Budget estimates include an assumption that additional expenditure of approximately 1% of total appropriations will be made in every year by use of the Treasurer's Advance.

Capacity for future capital works programs

The 2006-07 to 2008-09 forward year budget estimates include a provision for new capital works projects totalling approximately \$50m per annum. In addition, a further provision totalling \$31m per annum has been incorporated into agencies' 2006-07 to 2008-09 forward year budget estimates. This additional provision provides funding for capital upgrades. This includes capital works that extend the useful lives or improve the service delivery capacity of existing Territory assets.

Revenue Assumptions

The estimates of GST revenue from the Australian Government are based on the Australian Government Treasurer's *March 2005 Statement of Estimated Payments*, presented to the State and Territory Treasurers at the 2005 Treasurers' Conference. The SPP estimates are based on information provided by the Australian Government Department of Finance and Administration and reflect the Australian Government's 2004-05 Mid Year Economic and Fiscal Outlook.

Taxes, fees and fines, and other own source revenues are based on the economic assumptions discussed above. Revenues related to housing market activity, include conveyances and revenue from land sales, incorporate assumptions about conditions in the housing market.

The assumptions and outlook underpinning the conveyance revenue in 2004-05 are for a continued easing in turnover, coupled with a small increase in price. Across the forward years, activity is assumed to increase by around 3% per annum, while prices are assumed to increase at a rate slightly above the CPI.

