

CCI FLASH NOTE: Commonwealth budget, Oct 2020: Tracking better than the government's forecast profile ahead of a windfall from iron ore

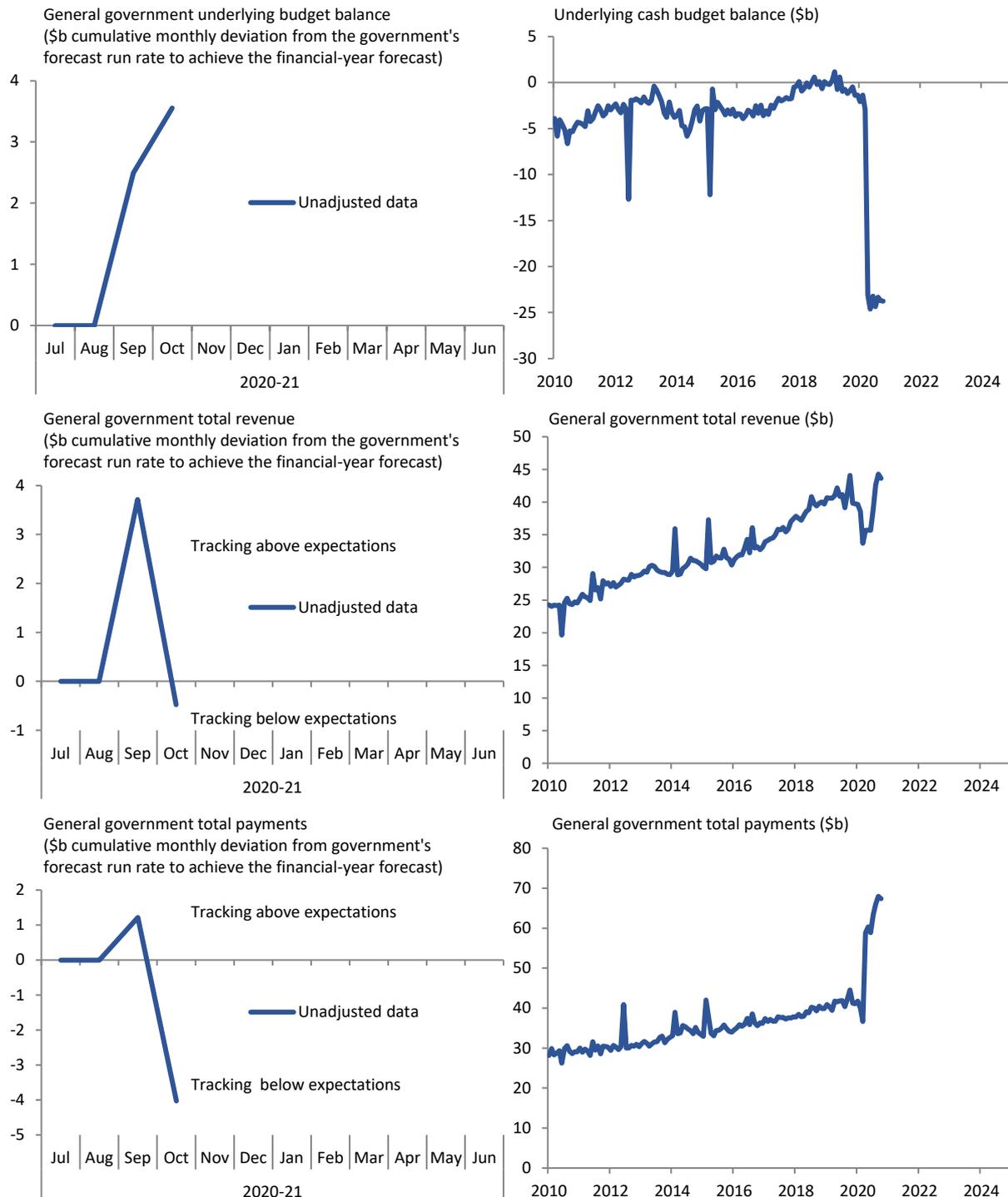
Treasurer Frydenberg is expected to publish a budget update this week, with the Mid-year Economic and Fiscal Outlook (MYEFO) reportedly due on Thursday. Treasury's strong preference would be to publish no change to the outlook given the full budget was released in October, but we think it will trim its forecast for an underlying cash deficit in 2020-21, revising it by about \$11bn from \$214bn to around \$203bn (or from 11.0 to about 10.4% of GDP), with an additional windfall in 2021-22 if iron ore prices stay high.

The anticipated revision reflects the net of:

- **A better-than-expected starting point of about \$3.5bn.** On CCI's seasonal adjustment, the underlying budget has averaged about \$24bn per month in the four months to October and is tracking about \$3.5bn better than the government had expected. This reflects underspending across nearly all types of expenditure, with welfare payments peaking in July and grants and subsidies looking to have peaked in September. Revenue has rebounded to pre-virus levels and is broadly in line with government expectations.
- **A large \$9bn windfall from an improving economy with less spending on the JobKeeper welfare payment.** The JobKeeper payment was [estimated](#) to be paid to about 4 million recipients by Q3 2020, 2.25 million by Q4 2020 and 1.75 million by Q2 2021 at a cost of \$65bn for 2020-21 as a whole. However, the treasurer [recently](#) said that about there were 0.7 million fewer participants than expected in October. Assuming this improvement is maintained into Q1, it would reduce the total cost of this key stimulus measure by about \$9bn for 2020-21.
- **Windfall company tax of \$1.5-2bn from high iron ore prices.** The price of iron ore is near \$US150/t, well above the budget's conservative [assumption](#) that it would fall to \$US55/t by Q2 2021. If the MYEFO assumes a similar rate of decline from this higher starting point then iron ore would deliver a windfall company tax gain of about \$8bn (the windfall is tempered by the recent appreciation of the exchange rate). This would boost taxes by about \$1.5-2bn in 2020-21, with the rest paid in 2021-22. There should also be a minor windfall from higher than assumed prices for LNG producers.
- **A temporary increase in spending of about \$3.5bn.** There are increased costs from the extension of the [JobSeeker Coronavirus Supplement](#) to welfare recipients and the [HomeBuilder](#) subsidy for the housing industry to Q1 2021. The extension of the welfare supplement should cost \$3.2bn, while the housing subsidy costs around \$0.2bn.

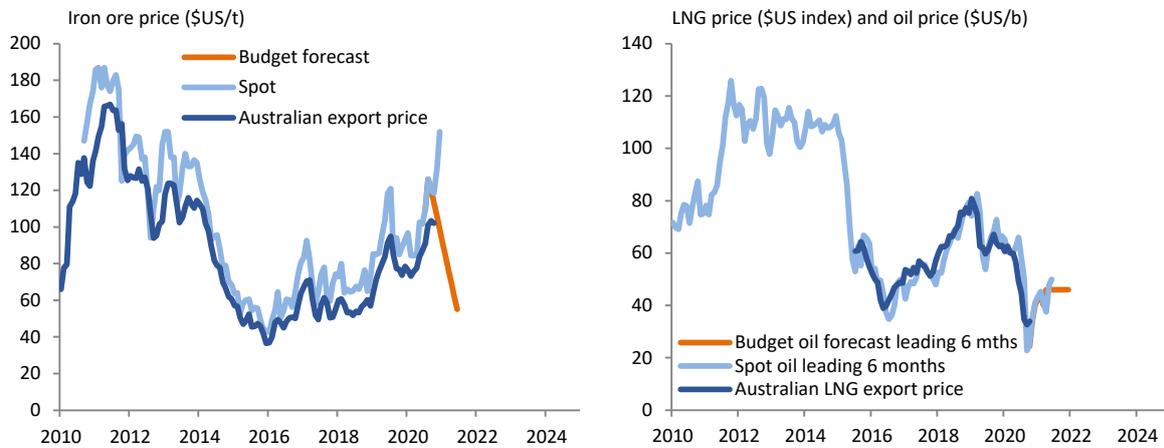
While mindful that some of the underspend in early 2020-21 could reflect timing issues given the sheer scale of the government's fiscal stimulus, CCI's tracking and seasonal adjustment of the monthly budget data suggests there is a risk that the deficit turns out better than the expected MYEFO revision, barring a setback on the health front. On the downside, Australia's trade relationship with China continues to deteriorate and creates additional uncertainty around the outlook for trade and the broader economy. Once the MYEFO is published, the Australian Office of Financial Management should update its funding task for 2020-21, where it [previously](#) estimated Treasury bond issuance of around \$240bn.

Figure 1: The Commonwealth budget is tracking better in the first four months of 2020-21 than the government had forecast because of lower payments



*Note: The cumulative deviation from the government's forecast run rate is the sum of unadjusted data in the financial year to date less the government's cumulative forecast for those months. The budget time series are seasonally adjusted by CCI.
 Source: Department of Treasury, Coolabah Capital*

Figure 2: Iron ore prices are substantially higher than the budget forecast, while oil prices are slightly higher



Source: Australian Bureau of Statistics, Department of Treasury, Coolabah Capital

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