

Federal Budget 2015 – 16

A Business Focus

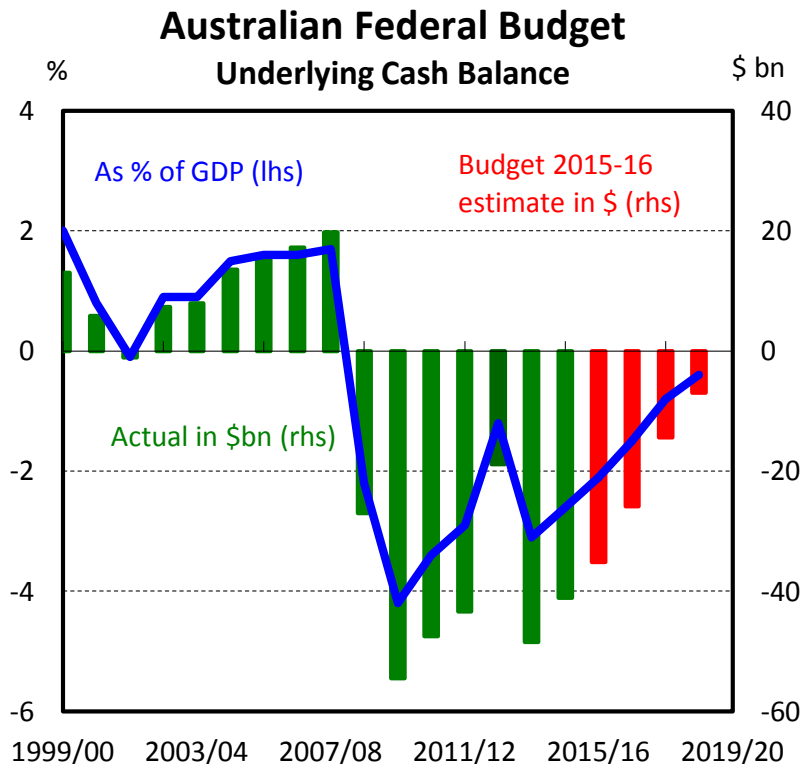
St. George Economics
May 2015

Outline

- The Federal Government released its Budget for 2015-16 on May 12.
- The deficits in 2015-16 and in following years were revised higher.
- Some of last year's unpopular measures have been abandoned.
- Weak profit and wage growth are weighing on revenues.
- Surplus is not expected till after 2020.



The Budget Bottom Line



- The Government is expecting a deficit of \$35.1bn in 2015-16 after a deficit of \$41.1bn in 2014-15.

- It is not a “slash and burn” budget, nor is it a “big spending” budget.

- This means that the direct contractionary impact on the economy will be modest. There should be some positive indirect impact via a lift in consumer sentiment.

Key Policies Affecting Businesses

Small Businesses

- The company tax rate will be cut from 30.0% to 28.5% for small businesses.
- Accelerated depreciation write off for assets costing under \$20k.
- Other measures to support small business.

Healthcare

- \$1.6bn for new and amended listings on the Pharmaceutical Benefits Scheme (PBS).
- \$962.8mn to be cut over five years across a range of health programmes.

Childcare

- A new Child Care Subsidy of up to 85% for family incomes of \$60k or less, and an annual cap of \$10k on family incomes of \$185,710 or more.

Research and Development

- A cap of \$100mn for R&D expenditure claimable on the concessional rate.
- Proceeding with a 1.5% reduction to the R&D tax offset to 43.5% for refundable tax offset and 38.5% for the non-refundable tax offset.

Infrastructure

- Up to \$5bn for Northern Australia Infrastructure Facility to provide concessional loans.

Foreign Investment

- New application fees on all real estate, business and agricultural foreign investment proposals from 1 December 2015.

Education

- \$843mn for 2016 and 2017 for preschool programmes.

Small Businesses – The Big Winners

- One of the headline acts was to reduce the company tax rate from 30% to 28.5% for small businesses with annual turnover below \$2 million from 2015-16.
- Unincorporated small businesses will receive a 5% discount on income tax payable on business income received, up to a total benefit of \$1,000 per year.
- Small businesses will receive an immediate tax deduction for assets costing less than \$20,000, up from \$1,000. The deduction is effective on assets acquired and installed ready for use now, until 30 June 2017.

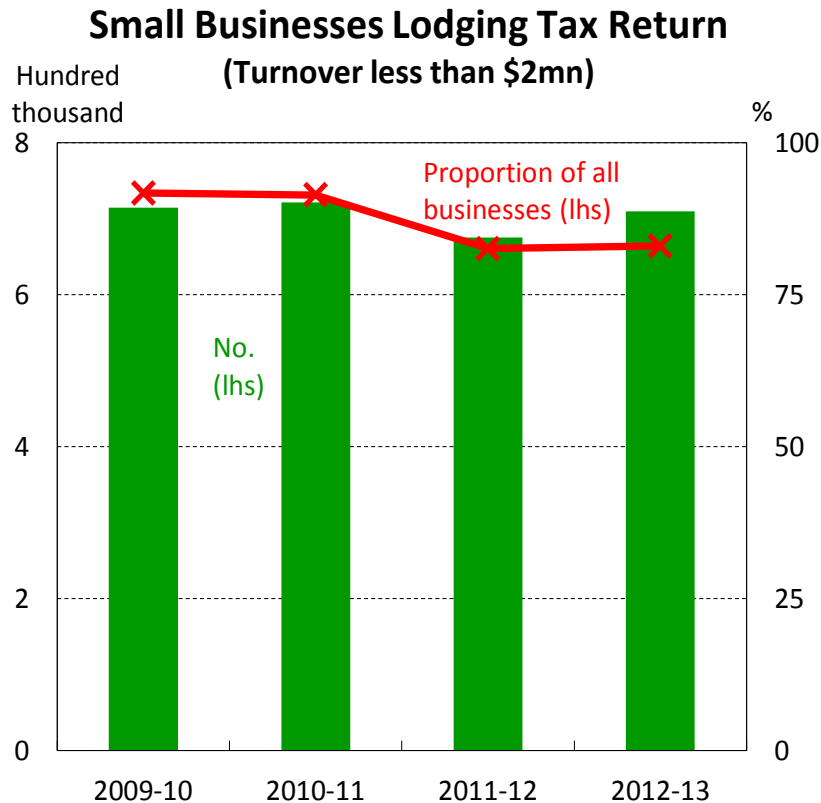


Small Businesses – Other Measures

- Allowing small businesses to immediately deduct professional services expenses associated with starting a new business such as professional, legal and accounting services. Previously, these were deducted over a five-year period.
- Allow small businesses (under \$2mn turnover) to change their legal structure without attracting a capital gains tax liability from 2016-17.
- Allow a fringe benefits tax exemption for small businesses (under \$2mn turnover) for more than one work-related electronic device from 1 April 2016.
- \$7.8mn over four years for ASIC to implement regulatory framework to facilitate the use of crowd-source equity funding.
- \$32.4mn over five years from 2014-15 for various government departments to streamline business registration.



What is a “Small Business”?



Source: Australian Taxation Office

- Most benefits are for businesses with under \$2 million annual turnover.
- Nearly 2 million businesses would qualify under this criteria, but less than half are likely to benefit from the government’s key measures (ie. have lodged a tax return).
- The measure to accelerate depreciation could bring forward some investment spending.

Industry Winners

- **Security and Defence** – Additional \$1.2bn (on top of existing \$1bn) for programmes including counter terrorism, border protection, intelligence collection. Pay rise for defence workers.
- **Pharmaceuticals** – new PBS listings (but higher prices for some drugs).
- **Agriculture** – \$271.8mn over four years from 1 July 2015 to assist farmers in drought-affected areas. Includes funding for concessional loans, social and mental health services and infrastructure. There will also be improved roads in Northern Australia.
- **Child Care/Early Childhood Education** – Child Care subsidy, preschool programmes funding, Nanny Trial.
- **Telecommunications** – \$131mn to upgrade systems to implement the Government's metadata retention policy.
- **Conservation** – extra \$100m in funding for the Great Barrier Reef .
- **Nuclear Science** – \$20.5mn in 2016-17 to the Australian Nuclear Science and Technology Organisation for the Australian Synchrotron.

Those Losing Out

- **Online Goods and Service providers** – GST will now be applied to digital products and services imported by consumers from 1 July 2017.
- **Multinationals** – “Google” Tax on 30 companies shifting profits to offshore subsidiaries.
- **Mid-sized Businesses** – Will no longer receive the reduction in company tax to 28.5%.
- **Resources** – Fly In Fly Out (FIFO) workers to lose beneficial zone tax offset.
- **Engineering Construction** – Aside from funding for Northern Australia, overall spending on new infrastructure was lacking. However, the Asset Recycling Initiative agreements with the States still stand.
- **Health Care/Not-For-Profit**– current fringe benefit tax (FBT) exemptions will be capped at \$5,000.
- **Health** – \$962.8mn to be cut over five years across a range of health programmes.
- **Research & Development** – A cap of \$100mn on eligible R&D which can be claimed at a concessional tax rate. Further, the government is proceeding with a reduction in the rate of R&D tax offset by 1.5 percentage points to 43.5% for the refundable tax offset and 38.5% for the non-refundable tax offset.
- **Innovation** – Reduced funding of \$31.7mn over three years for Commercialisation Australia, Enterprise Connect & Industry Innovation Precincts.

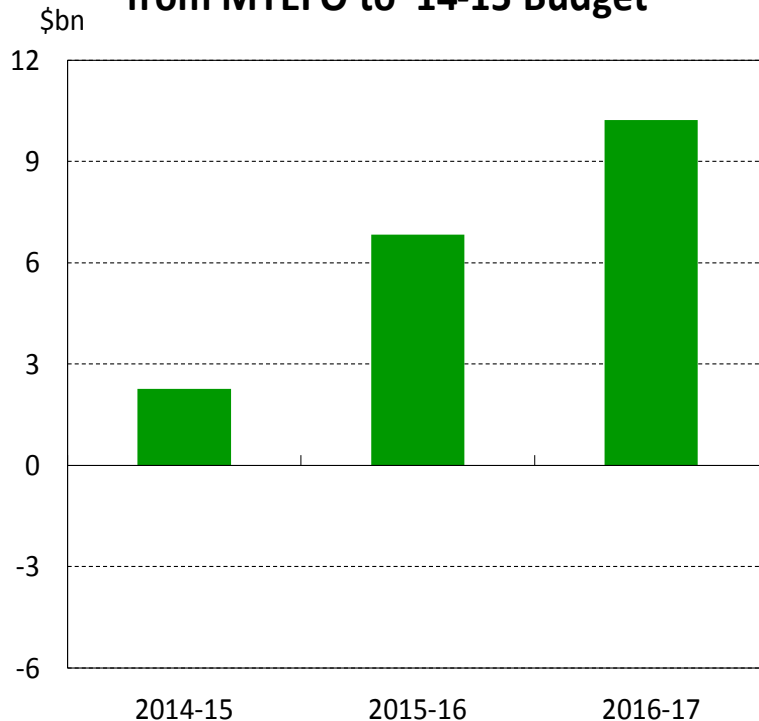
Other Measures

- Pension changes - Some will lose the part-pension, but poorer retirees receive an average pension increase of \$30 per fortnight,
- Parents on Employer-Paid Parental Leave – no ‘double dipping’.
- Working Holiday Makers – face higher tax rate (non longer access tax-free threshold, treated as non-residents for tax purposes).
- Graduates Living Overseas – will have to make HELP repayments.
- Older Job Seekers – Employers are now able to access \$10k subsidy over 12 months rather than 24 months. Payments can be made progressively.
- Measures with the aim to boost workplace productivity - Stronger penalties for job seekers who fail to comply with requirements, consolidating wage subsidy plans, and a National Work Experience program.

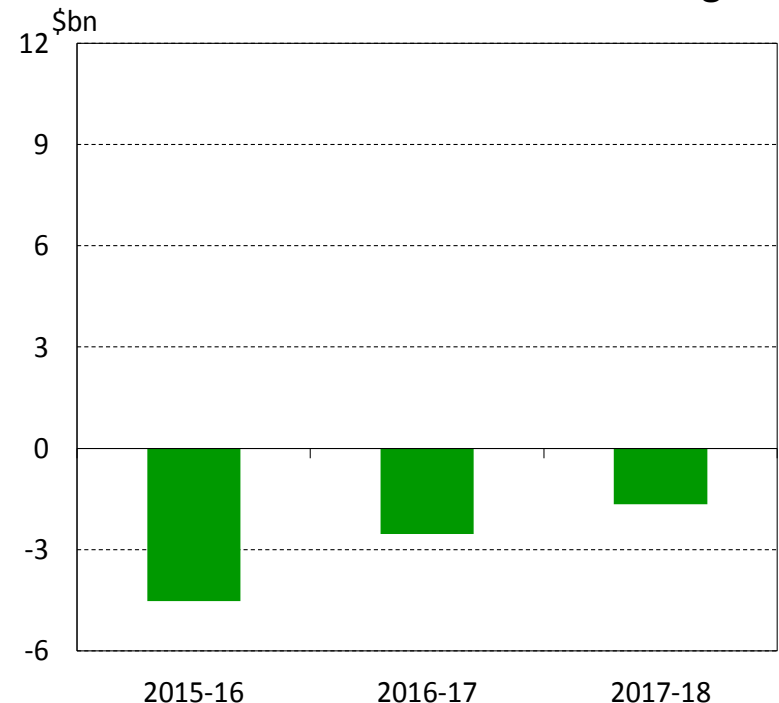


Fiscal Drag has been Reduced

**Fiscal Impact of Policy Decisions
from MYEFO to '14-15 Budget**



**Impact of Policy Decisions from
2014-15 MYEFO to 2015-16 Budget**



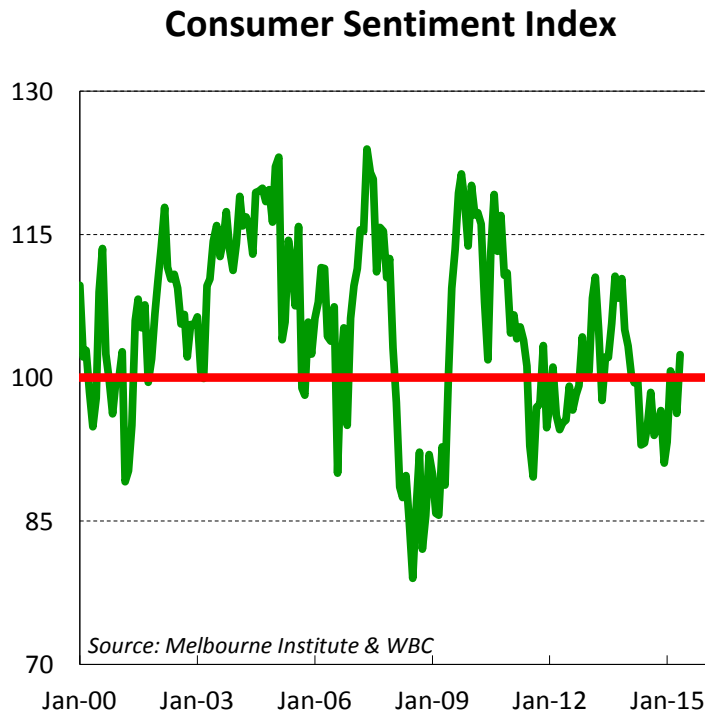
- The tightening impact has been pared back since the 2014-15 Budget.
- But the direct impact of fiscal policy is still contractionary.

It's All About Confidence

- While fiscal policy is still contractionary, the larger impact on the economy is likely to be through confidence.
- In 2014, confidence was dented following the 2014-15 Budget, particularly among consumers.
- This year, the 2015-16 Budget was not one of rapid repair nor sharp cuts to spending, and so has helped soothe concerns and boost consumer confidence.
- The passage of the Budget measures through Parliament and the playing out of the Budget in the media are likely to be longer-term drivers of confidence.

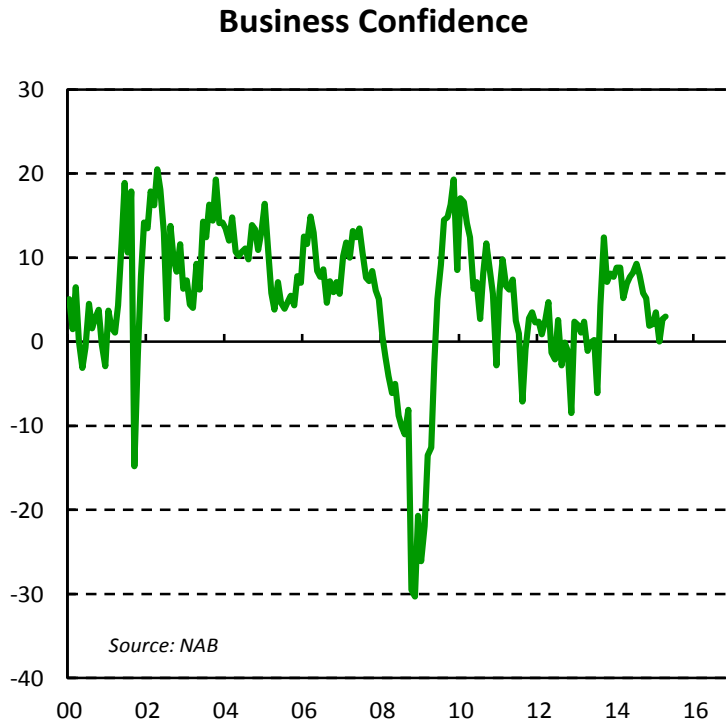


Consumer Confidence



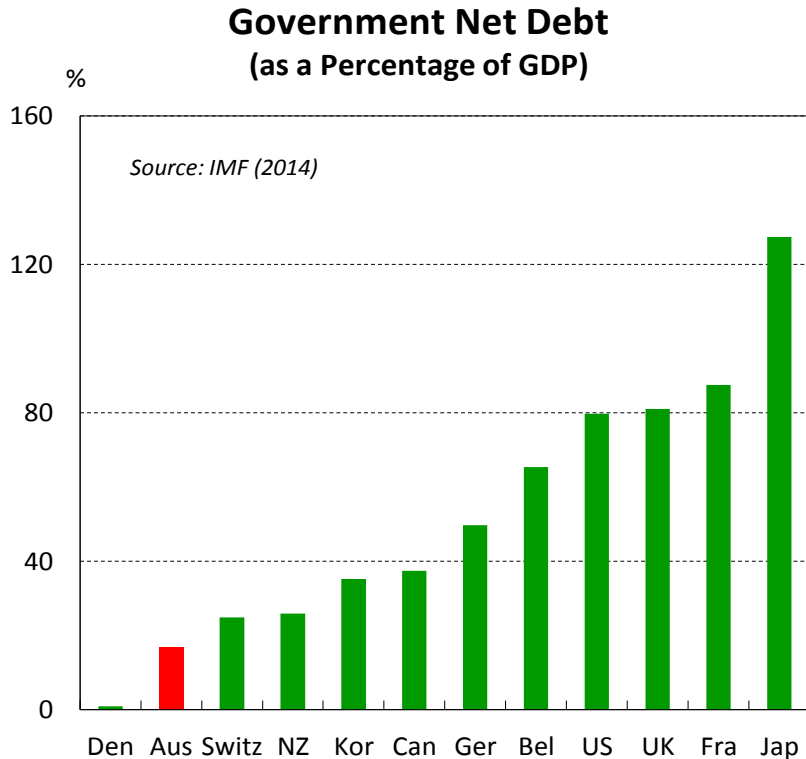
- Westpac-MI consumer confidence gained 6.4% in May, to a reading above 100 indicating more consumers are optimistic than pessimistic.
- This boost to confidence follows the release of the Federal Budget and an interest rate cut from the RBA in early May, but the details in the survey suggest the Budget played a larger role in the stronger confidence reading.
- Following the previous Budget in May 2014, consumer confidence fell 7.0%.

Business Confidence



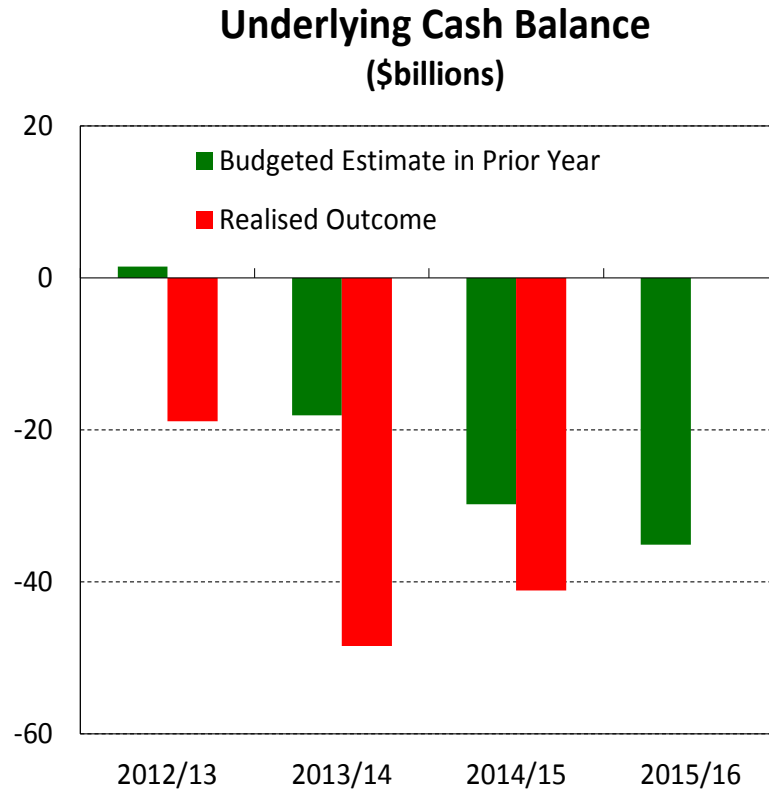
- We are yet to receive an update on business confidence following the Budget, although the measures assisting small business suggest that there will be some pick-up.
- A lack of business confidence or “animal spirits” has weighed on non-mining investment and economic growth.
- Hopefully the increase in consumer confidence in May can be sustained and will feed through to stronger business confidence.
- Following the previous Budget in 2014, NAB business confidence improved, rising from 6.9 to a reading of 7.7 in May.

What of the “Budget Emergency”?



- There was never a budget emergency to begin with.
- Net debt is expected to now peak at 18% of GDP, which is low by international standards.
- Structural issues in Australia's medium-term fiscal position require resolution.

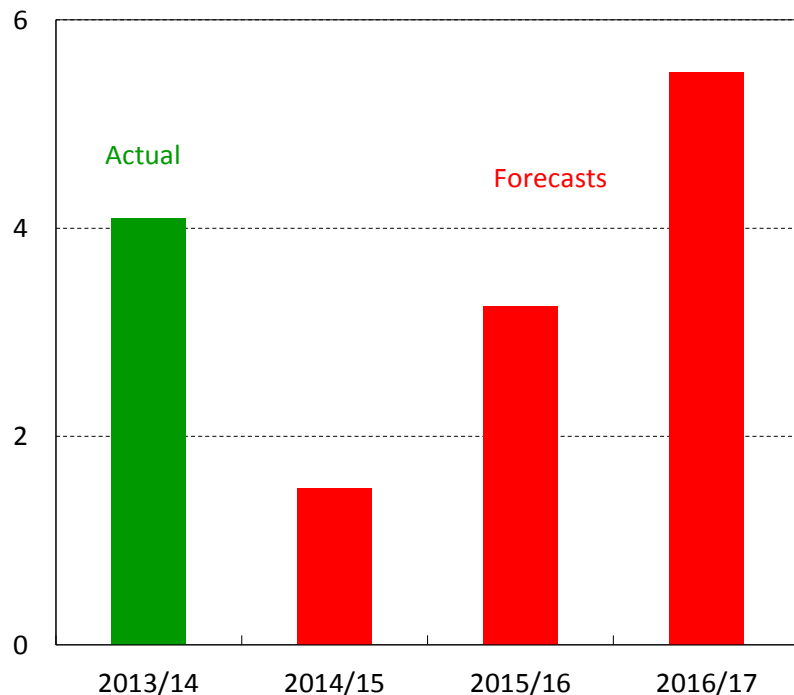
But It's a Slippery Slope



- Budget estimates have underestimated outcomes in recent years.

Depends on Growth Outcomes

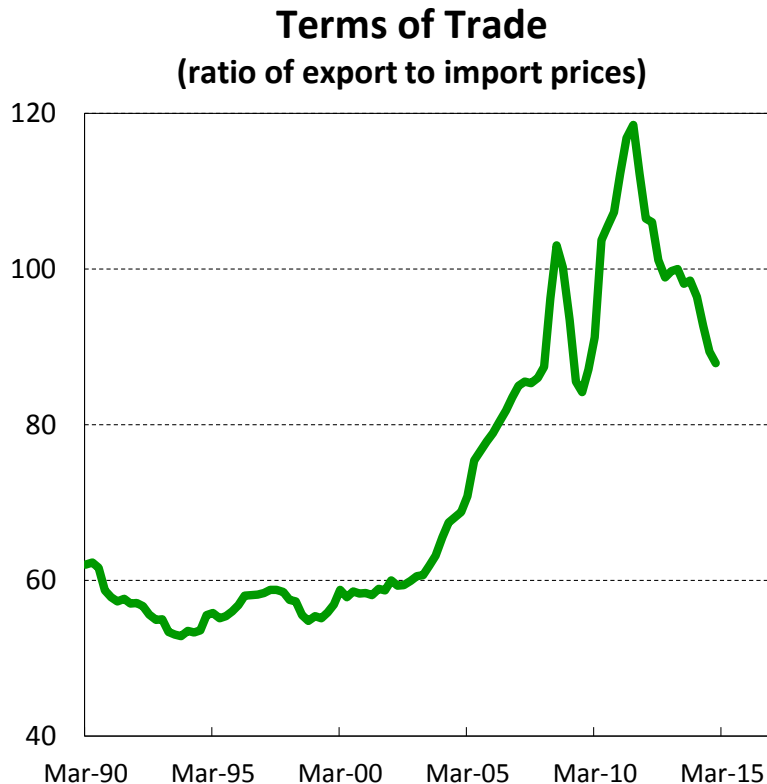
GDP Growth Treasury Forecasts
(Nominal, %)



- Nominal growth forecasts next year are conservative and plausible.
- However, the narrowing deficit in coming years depends highly on an expected pick up in growth.



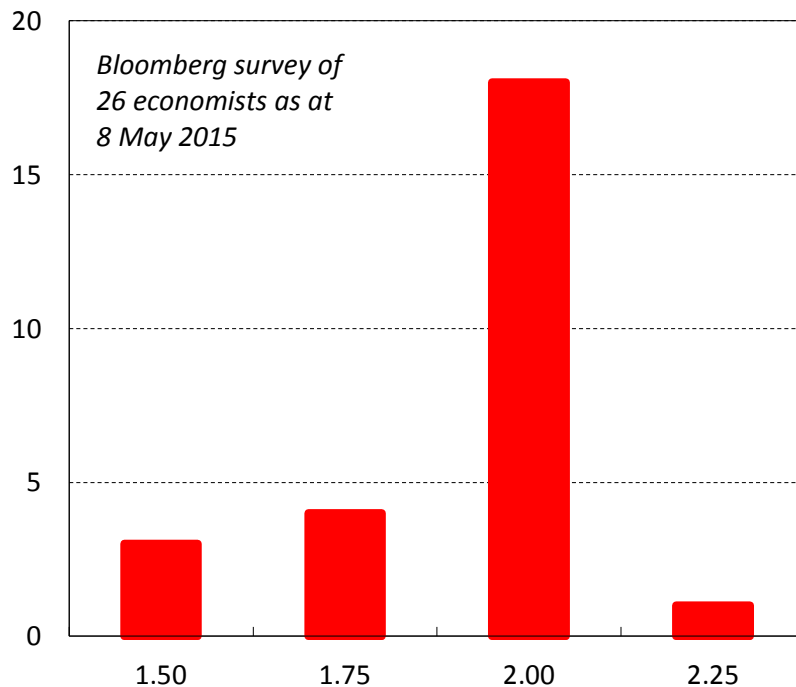
Terms of Trade – the Swing Factor



- A larger-than-expected decline in the terms of trade has been a key reason behind weak income and revenue growth.
- Iron ore and coal prices have been particularly weak.

Implications for Interest Rates

Where Will the Cash Rate Be at the End of 2015?



- We see limited impact on the outlook for official interest rates.
- The outlook continues to be for economic growth to remain below trend over much of 2015.
- Following two 25 basis point rate cuts this year in February and May, we expect the RBA will leave rates on hold for the remainder of this year.

Long-Run Issues Remain

- Ideally, the Budget should be in balance over the long-run.
- The sustainability of public finances with an ageing population is a key long-term issue.
- The Tax White Paper should raise some helpful discussion in providing more efficient ways of raising revenue.
- Bi-partisanship or constructive negotiations with a view to advancing the best interests of the nation would go a long way towards lifting productivity and business sentiment.



The Senate – Adding Uncertainty

Senate Composition From 16 March 2015	Seats
Coalition	33
Australian Labor Party	25
Greens	10
Palmer United Party (PUP)	1
Independents	4
Motoring Enthusiasts Party	1
Liberal Democratic Party	1
Family First	1
Senate	76

- Fewer unpopular policies suggest that this year's Budget will have an easier passage through Senate.
- However, the Senate remains a hurdle for many policies and continues to block some measures from last year's Budget.

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