



Victorian Budget 2021/22

# Creating Jobs, Caring for Victorians

STRATEGY AND OUTLOOK

Budget Paper No. 2

Presented by Tim Pallas MP  
Treasurer of the State of Victoria

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Authorised by the Victorian Government  
1 Treasury Place, Melbourne, 3002

Printed by Doculink, Port Melbourne

This publication makes reference to the  
2021/22 Budget paper set which includes:  
Budget Paper No. 1 – Treasurer's Speech  
Budget Paper No. 2 – Strategy and Outlook  
Budget Paper No. 3 – Service Delivery  
Budget Paper No. 4 – State Capital Program  
Budget Paper No. 5 – Statement of Finances  
(incorporating Quarterly Financial Report No. 3)

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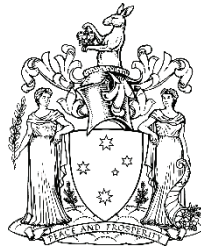
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ISSN 2204-9185 (print)  
ISSN 2204-9177 (online)  
Published May 2021

# Strategy and Outlook

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**2021-22**



Presented by

**Tim Pallas MP**

Treasurer of the State of Victoria

for the information of Honourable Members

**Budget Paper No. 2**



# TABLE OF CONTENTS

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<b>Chapter 1 – Economic and fiscal overview.....</b>	<b>1</b>
Victoria’s rapid economic recovery .....	1
Strong financial management.....	4
Debt management strategy .....	7
Summary of initiatives.....	11
<b>Chapter 2 – Economic context.....</b>	<b>19</b>
Victorian economic conditions and outlook .....	20
Other economic indicators.....	29
Australian economic conditions and outlook.....	38
International economic conditions and outlook.....	39
Risks to the Victorian outlook.....	42
<b>Chapter 3 – Investing early for better and fairer outcomes .....</b>	<b>45</b>
Mental health reform .....	47
Other early intervention investments and Partnerships Addressing Disadvantage...	52
<b>Chapter 4 – Budget position and outlook .....</b>	<b>57</b>
General government sector .....	58
Budget and forward estimates outlook.....	61
Fiscal risks .....	72
<b>Chapter 5 – Position and outlook of the broader public sector .....</b>	<b>77</b>
Non-financial public sector .....	79
State of Victoria .....	83
<b>Appendix A – Sensitivity analysis .....</b>	<b>87</b>
Fiscal impacts of variations to the economic outlook.....	88
Sensitivity to independent variations in major economic parameters .....	94
<b>Style conventions .....</b>	<b>97</b>



## **CHAPTER 1 – ECONOMIC AND FISCAL OVERVIEW**

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From 2014-15 to 2018-19, Victoria’s economic performance led the nation. Economic growth averaged 3.3 per cent and employment growth averaged 3.1 per cent a year over the five years to 2018-19, the strongest growth of all the states. Consistent with this, the Victorian unemployment rate had fallen to an 11-year low of 4.6 per cent in 2018-19 and remained below 5 per cent in December 2019 before the impacts of the 2019–2020 Victorian bushfires. However, in 2020, the coronavirus (COVID-19) pandemic had a significant impact on the Victorian economy – as it did on economies around the world – with the first economic downturn in 28 years and a fall in employment of 241 000 from March to September 2020.

The State’s economic recovery is now well underway, with employment and workforce participation both already recovered to pre-coronavirus (COVID-19) levels. More than 200 000 jobs have been created in Victoria, well ahead of the interim employment target in the Government’s *Jobs Plan*, announced as part of the *2020-21 Budget*.

Indeed, despite a longer period of public health restrictions in Victoria during 2020 – essential to save lives and underpin sustainable economic recovery – by early 2021 Victoria’s employment recovery had broadly caught up to that of the rest of Australia. The strong rebound in employment has led to a fall in the unemployment rate, which had declined to 6.1 per cent in March 2021 from a peak of 7.5 per cent in June 2020.

Economic activity also rebounded strongly in the December quarter 2020 with the easing of public health restrictions. Momentum has continued into the March quarter 2021, with retail spending at elevated levels, business conditions at around three-year highs, elevated consumer and business confidence, and a strengthening housing market.

The outlook for the Victorian economy is positive, underpinned by high levels of government support, low interest rates, the roll-out of vaccines – globally and domestically – and elevated levels of consumer and business confidence. However, the nature of the coronavirus (COVID-19) pandemic means that risks to the economic outlook remain elevated.

### **VICTORIA’S RAPID ECONOMIC RECOVERY**

The coronavirus (COVID-19) pandemic has had a significant impact on the Victorian economy since early 2020. Economic output and employment contracted sharply in the June quarter 2020 as public health restrictions were introduced, and weakened again in the September quarter alongside Victoria’s second phase of public health restrictions.

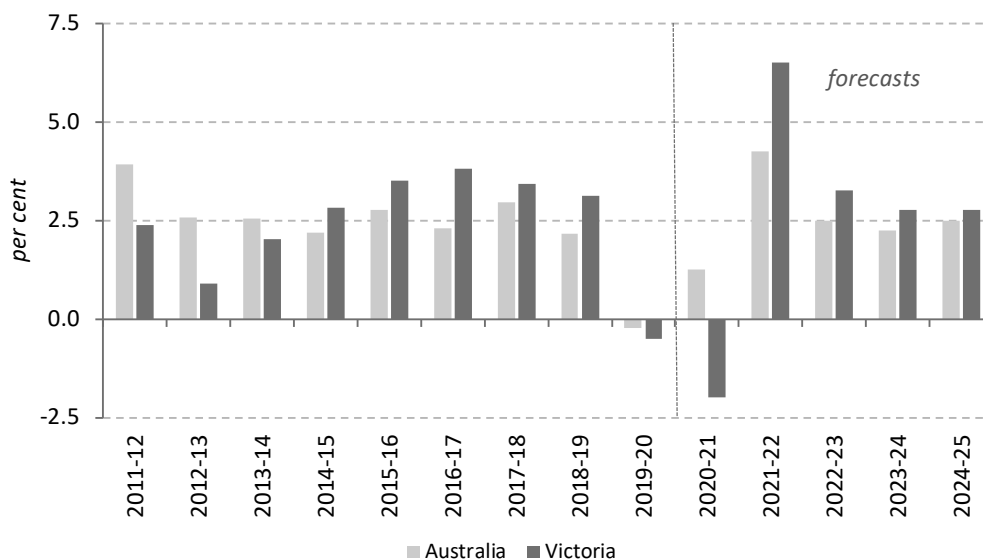
These restrictions were necessary to save lives, limit the spread of COVID-19 and enable sustained economic recovery. With restrictions being eased through the latter part of 2020, activity and employment rebounded strongly in the December quarter. By March 2021, employment had recovered to pre-coronavirus (COVID-19) levels.

Victoria’s recovery is now well underway and the outlook for the economy is positive. Business and consumer confidence are elevated, household balance sheets in aggregate are strong and monetary policy remains highly supportive. The Australian economy is also recovering, and the global economic outlook has improved.

Government support through public spending has helped cushion the economy while private demand contracted during the COVID-19 pandemic. Victorian, Commonwealth and local government support remain important as the economy transitions back to private sector-led growth. This budget continues to support the economic recovery, with the Government investing in services and infrastructure to both underpin the current recovery and drive future economic growth. Priorities for this budget include rebuilding the mental health system, investing to protect vulnerable children and support their families, and continuing the Big Build to deliver the roads, rail, schools and hospitals the State needs.

Victorian gross state product (GSP) is forecast to increase by 6.5 per cent in 2021-22. This follows an estimated fall of 2.0 per cent in 2020-21, and a decline of 0.5 per cent in 2019-20 due to the impact of the coronavirus pandemic on the June quarter 2020 (see Chart 1.1).

**Chart 1.1: Real economic growth, actual and forecast, Victoria and Australia<sup>(a)</sup>**



Source: Australian Bureau of Statistics; Department of Treasury and Finance; Commonwealth Treasury

Note:

(a) Forecasts are rounded to the nearest 0.25 percentage points.



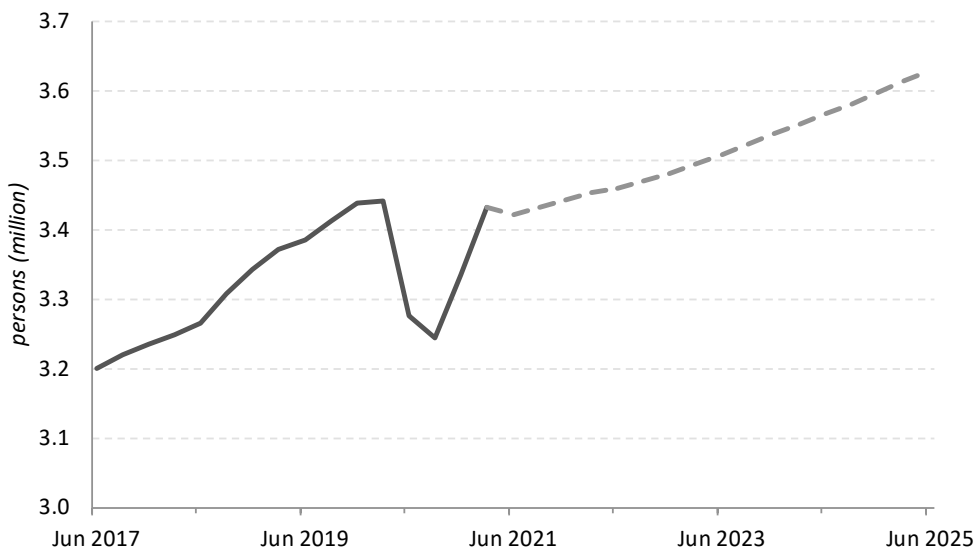
Employment rebounded strongly in the December quarter as the second phase of Victoria’s restrictions were eased, and there were further gains in the March quarter (see Chart 1.2). Overall, employment rose by 243 000 persons between September 2020, the low point for employment, and March 2021. The unemployment rate has also declined sharply, although it remains above pre-coronavirus (COVID-19) levels.

The Government’s *Jobs Plan*, announced as part of the *2020-21 Budget*, included a target to create 400 000 jobs by 2025, with half of these by 2022. The strength of the Victorian economic recovery means the interim target has already been met. Employment among women has rebounded to pre-coronavirus (COVID-19) levels, despite women being disproportionately affected by job losses in 2020. The proportion of young people in employment has now also recovered to around pre-coronavirus (COVID-19) levels. In March 2021, Victoria’s labour force participation rate was at a new record high.

Employment is forecast to grow by 2.5 per cent in 2021-22. The unemployment rate has likely already peaked. It could rise moderately in the short term due to the end of the JobKeeper wage subsidy in late March 2021, but is then expected to edge lower, averaging 5.75 per cent in 2021-22, from 6.5 per cent in 2020-21.

Nevertheless, some regions and sectors of the economy are still experiencing higher rates of unemployment. The nature of the COVID-19 pandemic also means that risks to the economic outlook remain elevated. Overall, however, the outlook for the Victorian economy is positive.

**Chart 1.2: Victorian employment, quarterly, actual and forecast**



Source: Australian Bureau of Statistics; Department of Treasury and Finance

## STRONG FINANCIAL MANAGEMENT

Prior to the coronavirus (COVID-19) pandemic, the Government demonstrated its strong financial management by adhering to a clear and robust fiscal framework, including operating surpluses and maintaining debt at a sustainable level while delivering improved services and infrastructure.

However, in 2020 – like all states and territories – the pandemic severely impacted the State’s financial position and outlook. In the *2020-21 Budget*, the Government forecast operating deficits and increasing net debt in each year over the forward estimates. This was the result of the combined impact of lower revenue and increases in critical expenditure to support the State’s health and economic recovery effort.

The Government prioritised the use of its balance sheet to support the Victorian community. This approach was consistent with stimulus approaches in Australia and around the world and was supported by the Governor of the Reserve Bank of Australia who encouraged governments to stimulate the economy through increased borrowings.

Economic indicators show that the Government’s stimulus strategy is working, with the economy rebounding strongly. The *2021-22 Budget* forecasts significant improvement in the State’s key fiscal aggregates over the budget and forward estimates. This improvement is the result of the Government’s comprehensive and deliberate fiscal strategy set out in the *2020-21 Budget*. This strategy focuses on the medium term, and involves four steps:

- **Step 1:** creating jobs, reducing unemployment and restoring economic growth;
- **Step 2:** returning to an operating cash surplus;
- **Step 3:** returning to operating surpluses; and
- **Step 4:** stabilising debt levels.

The *2021-22 Commonwealth Budget* was released on Tuesday 11 May 2021. The Budget does not account for the grants and funding agreements announced by the Commonwealth Government, which are subject to negotiation and confirmation with the Victorian Government.

Many of the infrastructure initiatives and funding agreements are contingent on the Victorian Government sharing the costs. As such, Victoria will consider these initiatives and their suitability with the State’s forward infrastructure agenda.

## Progress towards achieving the Government's fiscal strategy

The first step, creating jobs, reducing unemployment and restoring economic growth was a key focus in the *2020-21 Budget* and remains a focus in this budget. There continues to be a role for the Government in supporting the economic recovery. This continued support will, in the longer term, help support a return to a stronger and more sustainable fiscal position. It is also consistent with guidance from the Reserve Bank of Australia and the International Monetary Fund that have both cautioned against prematurely withdrawing policy support measures before recovery is fully entrenched.

The second step in the Government's fiscal strategy, returning to an operating cash surplus, is an important step because it means the State is generating sufficient cash inflows to offset its cash outflows on operating activities, a key pillar of a jurisdiction's fiscal sustainability.

From 2022-23 the Government is forecasting a return to operating cash surpluses, a significant milestone, and an improvement on the State's position since the *2020-21 Budget*. Revenue forecasts have recovered – in part through the Government's deliberate interventions in the economy, building confidence and supporting jobs. These interventions are likely to have sustained influence on the economy, with many of the Government's investments scheduled to continue flowing through the economy over the next couple of years.

In this budget, the Government has also strengthened its revenue base through the introduction of new initiatives. These targeted initiatives recognise that some sectors of the economy were not as adversely impacted by COVID-19, and ensure these sectors contribute to the recovery.

On the expenditure side, consistent with the key principles established in the *2020-21 Budget*, this budget sees the tapering of expenditure in the near term. New operating expenditure initiatives over the budget and forward estimates are supported through existing or new funding mechanisms, not by increasing the Government's borrowings over the budget and forward estimates. The Government will implement new savings and efficiencies to help moderate expenditure growth while still delivering improvements in important services.

The third step, returning to an operating surplus, remains a key priority for the Government. An operating surplus is the important next step as it is where government generates sufficient revenues to not just cover its operating expenditure, but also support the replacement of existing assets.

The operating deficit is now significantly smaller in each year over the budget and forward estimates, relative to the *2020-21 Budget*. The savings, efficiencies and new revenue initiatives will gradually take effect from 2021-22 onwards, supporting continued economic recovery and progress against the Government's fiscal strategy.

There has also been progress in the fourth step in the strategy, stabilising net debt. The improvements to the Government's operating position have flowed through to net debt. Net debt is now lower in each year than was forecast in the *2020-21 Budget*. In the *2020-21 Budget*, net debt was forecast to increase to around \$155 billion by 30 June 2024, but this increase is now not forecast until 30 June 2025.

## Financial position

Total revenue for the general government sector is expected to be \$74.6 billion in 2021-22, an increase of \$3.3 billion compared with the *2020-21 Budget*. Total revenue is expected to grow by an average of 4.6 per cent a year over the forward estimates to \$85.3 billion in 2024-25.

Total expenditure is expected to reach \$86.2 billion in 2021-22, before reducing by 2.9 per cent in 2022-23, reflecting the targeted and short-term nature of initiatives to fund the public health response and support the economy from the impacts of the pandemic. Expenditure growth is forecast to moderate over 2023-24 and 2024-25, with total expenditure reaching \$87.4 billion in 2024-25.

This is contributing to improvements in the State's operating cash position (net cash flows from operating activities), with an operating cash surplus forecast of \$1.1 billion in 2022-23 and increasing to \$3.0 billion in 2024-25.

The State is forecasting operating deficits (net result from transactions) over the budget and forward estimates. However, these estimates reflect an improvement relative to the *2020-21 Budget*.

Net debt is now lower in each year of the forward estimates than was forecast in the *2020-21 Budget*, principally due to improvements in the operating position.

**Table 1.1: General government fiscal aggregates**

	<i>Unit of measure</i>	<i>2019-20 actual</i>	<i>2020-21 revised</i>	<i>2021-22 budget</i>	<i>2022-23 estimate</i>	<i>2023-24 estimate</i>	<i>2024-25 estimate</i>
Net result from transactions	\$ billion	(6.5)	(17.4)	(11.6)	(3.8)	(2.1)	(2.1)
Net cash flows from operating activities	\$ billion	(2.9)	(17.4)	(2.0)	1.1	2.4	3.0
Government infrastructure investment <sup>(a)(b)</sup>	\$ billion	12.0	14.5	24.2	21.7	22.7	21.6
Net debt	\$ billion	44.3	77.5	102.1	120.0	138.3	156.3
Net debt to GSP <sup>(c)</sup>	per cent	9.5	16.7	20.3	22.7	24.9	26.8

Source: Department of Treasury and Finance

**Notes:**

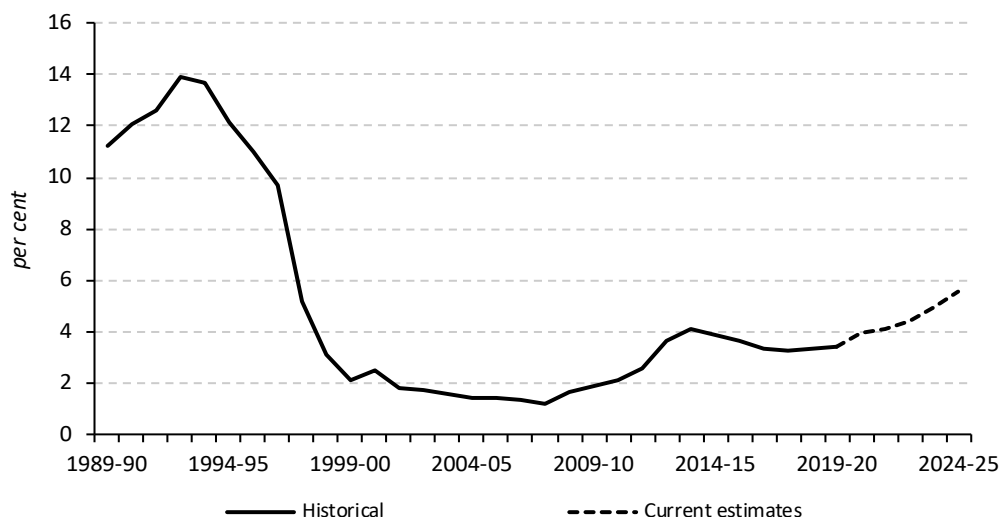
- (a) Includes general government net infrastructure investment and estimated construction costs for public private partnership projects.
- (b) Includes the estimated private sector construction related expenditure associated with the North East Link held in the public non-financial corporations (PNFC) sector.
- (c) The ratios to GSP may vary from publications year to year due to revisions to the Australian Bureau of Statistics GSP data.

## DEBT MANAGEMENT STRATEGY

Stabilising debt – the last step in the Government’s fiscal strategy – is important as debt will continue to grow as a percentage of GSP, until operating surpluses are at a level which limits the growth in debt to the growth rate of GSP.

The increase in debt is manageable, as current low interest rates mean that interest expense as a proportion of total budget revenue is much lower than previously. The Reserve Bank of Australia has indicated that interest rates are expected to remain low for an extended period. This means that interest expense as a proportion of revenue is forecast to remain at moderate levels by historical standards, as highlighted in Chart 1.3.

**Chart 1.3: Interest expense to revenue ratio <sup>(a)</sup>**



Source: Department of Treasury and Finance

Note:

(a) Interest expense to revenue ratio prior to 1996-97 has been calculated on a cash basis, as accrual accounting was implemented from 1996-97 onwards.

While government bond yields are at historically low levels (see Chart 1.4) and are expected to remain low in the medium term, the potential for long-term bond rates to increase presents a risk to the budget of increased interest expense. This risk is lessened by a debt management strategy which smooths the impact of interest rate movements by spreading largely fixed rate borrowings evenly over the long-term. This strategy provides greater certainty to the Government that interest expense remains stable over the medium term.

**Chart 1.4: 10-year Victorian government bond yields**



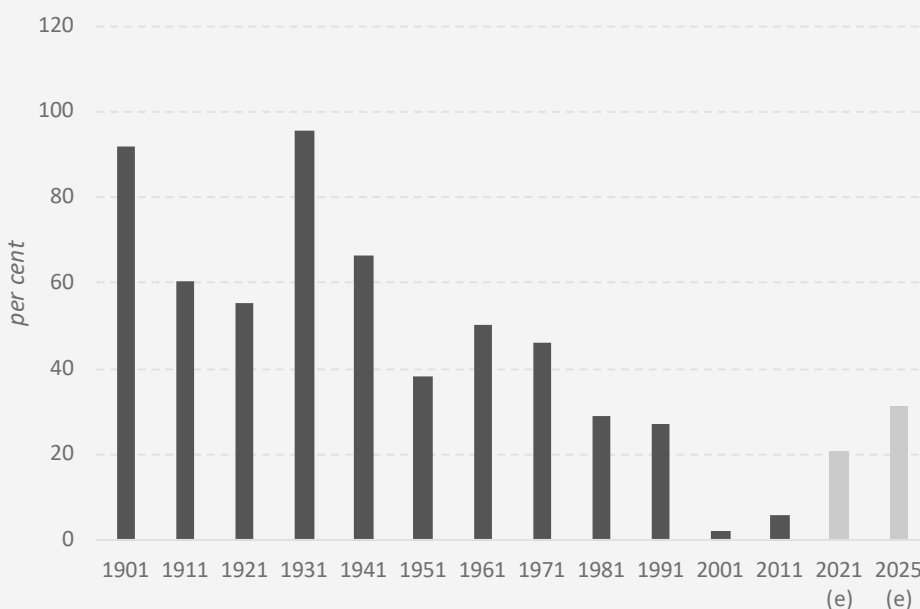
Source: Treasury Corporation of Victoria

### Box 1.1: Historical Victorian debt

The pandemic has had a significant impact on the Victorian economy and, through the Government's actions to respond to and recover after the pandemic, on Victoria's debt. The impacts of this event on the Victorian debt position should be considered in the context of how Victoria's fiscal position changed in response to other notable events over the past century.

Chart 1.5 shows net debt to GDP ratios at ten-year intervals over the 120 years since Federation. While debt has increased over the past decade, primarily as a result of infrastructure investment and the pandemic, the increase is still moderate relative to debt incurred in varying circumstances across earlier decades.

**Chart 1.5: Historical Victorian net debt to GDP for the non-financial public sector (NFPS), 1901 to 2025**



Sources: NFPS net debt – Department of Treasury and Finance. GSP – from 1990, ABS; pre-1990, Annual Estimates of Gross Domestic Product, Australian Colonies/States, 1861-1976/77, W. A. Sinclair, Monash University, published 30 September 2009

Notes: It is not possible to derive fully consistent NFPS net debt or GSP time series from 1901 to the present because of incomplete data. The Department of Treasury and Finance has used published NFPS net debt figures for recent decades and has assembled earlier data from various Victorian Government published sources. For pre-1990 GSP estimates, the methodology is based on N.G. Butlin's in Australian Domestic Product, Investment and Overseas Borrowing 1861-1938/39 (Cambridge University Press, 1962).

In general terms, there has been a gradual reduction in the Victorian net debt to GDP ratio over the past century.

## Longer-term objectives and targets

In the context of a changed economic landscape, following the global recession stemming from the COVID-19 pandemic and increases in expenditure to fund a significant health and economic response, the Government is taking steps to progressively realign expenditure to target areas of highest priority.

The Government will continue to improve the effectiveness of departmental spending and ensure expenditure is consistent with key service delivery priorities.

A range of expanded revenue initiatives in this budget recognise the gradual need to diversify State-sourced revenue. These initiatives will gradually take effect from 2021-22 onwards, supporting a return to operating cash surpluses by 2022-23.

The long-term financial management objectives remain unchanged from the *2020-21 Budget*.

**Table 1.2: Long-term financial management objectives**

<i>Priority</i>	<i>Objective</i>
Sound financial management	Victoria's finances will be managed in a responsible manner to provide capacity to fund services and infrastructure and support households and businesses in the economic recovery at levels consistent with sound financial management.
Improved services	Public services will improve over time.
Building infrastructure	Public infrastructure will grow steadily over time to meet the needs of a growing population.
Efficient use of public resources	Public sector resources will be invested in services and infrastructure to maximise the economic, social and environmental benefits.
A resilient economy	Increase economic resilience by supporting an innovative and diversified economy that will unlock employment growth, long-term economic growth and productivity in Victoria.

Progress towards these financial management objectives is supported by the measures and targets in Table 1.3. These measures and targets are also unchanged from the *2020-21 Budget*.

**Table 1.3: Financial measures and targets for the 2021-22 Budget**

<i>Financial measures</i>	<i>Target</i>
Net debt to GSP	General government net debt as a percentage of GSP to stabilise in the medium term.
Interest expense to revenue	General government interest expense as a percentage of revenue to stabilise in the medium term.
Superannuation liabilities	Fully fund the unfunded superannuation liability by 2035.
Operating cash surplus	A net operating cash surplus consistent with maintaining general government net debt at a sustainable level after the economy has recovered from the coronavirus (COVID-19) pandemic.



## **Budget reform**

The Government is committed to ensuring expenditure is targeted to areas of highest priority to deliver value for money and the greatest possible economic and social benefits for all Victorians. A range of budget reforms will be gradually implemented from 2021-22 onwards to support this objective.

This includes a shift towards a stronger social investment approach as part of this budget. Over the medium term, the Government aims to embed a social investment approach, progressively focusing expenditure towards earlier interventions, with the aim of improving outcomes for Victorians and reducing the pressure of acute service demand on the budget.

Structural improvements to provide greater expenditure oversight and performance monitoring at a program level across departments will also be implemented from 2021-22.

## **SUMMARY OF INITIATIVES**

Consistent with the Government's fiscal strategy, this budget focuses on consolidating Victoria's rapid economic recovery and growing employment – building a strong economic foundation.

This budget invests responsibly to deliver the services and infrastructure Victorians need – with initiatives to transform Victoria's mental health system, invest in early childhood and schools, support vulnerable children, women and families and build strong and safe communities. It continues to support the health system as Victoria emerges from the coronavirus (COVID-19) pandemic and invests in the transport that connects Victoria. These investments have the dual benefit of improving services for Victorians, while sustaining and creating jobs.

This budget provides \$19.0 billion over five years in output spending and \$7.1 billion of investments in new and improved assets - creating jobs, continuing to drive Victoria's economic recovery, and supporting the mental health and wellbeing of all Victorians.

The investments made by the Government in this Budget will support on average 38 000 jobs per year over the next four years. This includes around 3 000 jobs in our mental health system and around 1 000 to support our most vulnerable children, including in our child protection workforce.

## Transforming Victoria’s Mental Health system

The *2021-22 Budget* provides \$3.8 billion to transform the way mental health and wellbeing support is delivered in Victoria, consistent with the recommendations of the Royal Commission into Victoria’s Mental Health System.

This budget invests in mental health services across Victoria. Funding of \$264 million is provided for 20 new local services to provide community-based care for adults, along with \$954 million to establish 22 reformed area mental health and wellbeing services. A further \$370 million is provided for acute bed-based services. This includes continuing the Hospital in the Home program, an innovative alternative to hospital-based treatment. Improved mental health services will be accessible across the State, including in rural and regional Victoria.

A further \$842 million is provided for mental health and wellbeing support for children, young people and families. This investment will see the establishment of 13 reformed and expanded infant, child and family mental health and wellbeing services and three new multi-disciplinary hubs across the State, and 13 reformed and expanded Youth Area Mental Health Services. Funding of \$16 million is provided to establish four new Hospital Outreach Post-suicidal Engagement (HOPE) sites specifically designed for young people.

The *2020-21 Budget* funded the Big Housing Build to deliver 9 300 new social housing homes – including 2 000 for Victorians living with mental illness. The *2021-22 Budget* provides \$46 million to provide these Victorians with mental illness the mental health and wellbeing support they need to stay in housing and have the best possible life outcomes. This includes funding to co-design and plan for a further 500 housing places for young people living with mental illness.

The Government is supporting families and carers, with \$93 million in dedicated funding, including establishing eight carer-led centres that will provide practical help, through short-term respite and support groups.

These reforms will create significant economic benefit – reducing some of the \$14.2 billion in annual economic costs of poor mental health estimated by the Royal Commission into Victoria’s Mental Health System – and enabling more participation in the economy from Victorians whose mental health is improved by the Government’s investment.

The Government’s record investment in the mental health system will create 3 000 jobs in the sector. Victoria will need a strong pipeline of future workers, and this budget funds \$206 million to provide training support – including 120 graduate placements for nurses, 140 postgraduate mental health scholarships, 60 new graduate placements for allied health professionals and additional rotations for psychiatry.

The Royal Commission into Victoria’s Mental Health System recommended a new approach to mental health funding. This budget secures long-term funding for mental health reform by introducing a Mental Health and Wellbeing Levy on businesses with payrolls over \$10 million from 1 January 2022. This will generate sustainable and dedicated funding to be invested into the mental health system.

## Strong and responsive health sector

In the *2020-21 Budget*, the Government invested to control the spread of COVID-19 and equip health, ambulance and hospital services to care for Victorians. The *2021-22 Budget* continues this work, committing \$7.1 billion to health services and health infrastructure.

This budget provides \$1.3 billion to continue the public health response to COVID-19. An additional \$50 million is provided to support establishing the capability to manufacture mRNA vaccines here in Victoria, the first mRNA manufacturing capability in the southern hemisphere. This investment will help to provide certainty of supply of new vaccines in Victoria while creating local jobs.

Funding of \$3.7 billion will help the health system to recover from the challenges of COVID-19, and fund more emergency department staff, highly specialised therapies and support new wards as they open. The Government will also invest \$1.2 billion in building and upgrading hospitals and health care infrastructure across the State.

The Government is investing \$70 million to establish free public in-vitro fertilisation (IVF) services in Victoria to support 4 000 patients each year once fully operational. This includes \$3.5 million to deliver Australia's first public sperm and egg bank.

The Government recognises the need for high quality and safe public aged care services to support the health and wellbeing of Victorian seniors. Funding of \$94 million is provided for public aged care services. This includes funding to build a 50-bed aged care facility at Rutherglen, as well as to plan and design redevelopment of facilities at Cohuna and Camperdown.

## Continuing to drive Victoria's economic recovery

The *2021-22 Budget* continues to invest in Victoria's recovery from the COVID-19 pandemic, building on the progress made delivering the Government's *Jobs Plan* (see Box 1.2).

The creative and tourism sectors were particularly impacted by COVID-19. This budget invests \$288 million to support and create jobs, through a new *Creative State* strategy. This includes \$121 million for the Victorian screen industry, including funding to revitalise the Melbourne International Film Festival, and \$34 million to revitalise Victorian cultural institutions including Melbourne Museum. In addition, \$160 million will support the recovery of the tourism sector, promoting Victoria's strengths as a visitor destination and attracting new visitors to the State.

This budget provides \$107 million in additional support for business recovery in Melbourne's central business district (CBD). This includes a new CBD Dining Experiences Scheme to encourage Victorians to support city cafes and restaurants. A \$100 million investment to create the Melbourne City Revitalisation Fund will be matched by the City of Melbourne, creating a \$200 million pool to renew city spaces.

This budget is also supporting CBD activity with targeted tax relief. A temporary land transfer duty concession for new residential properties valued up to \$1 million in the Melbourne local government area will reduce costs for home buyers and support the construction sector. In addition, payroll tax cuts will be brought forward to 1 July 2021, supporting thousands of businesses across Victoria.

### **Box 1.2: Jobs Plan progress**

The *2020-21 Budget* funded a targeted, complementary set of initiatives to support Victoria's economic recovery after the coronavirus (COVID-19) pandemic. Together these initiatives formed the *Jobs Plan*. Key initiatives from the *Jobs Plan* are underway and the Government's interim target of creating 200 000 jobs by 2022 has already been surpassed.

Thousands of Victorian businesses received support to stay open and adapt to COVIDSafe requirements through multiple *Jobs Plan* initiatives. \$2.6 billion has been paid out to 134 000 individual businesses in the three rounds of the *Business Support Fund*. A further \$262 million has been provided through cash grants and cash flow support from *Business Resilience Package* initiatives.

The \$2 billion *Breakthrough Victoria Fund* has appointed an interim board and will soon finalise an investment plan which will support research and innovation across the State. The focus industries will include health and life-sciences, agri-food, advanced manufacturing, clean economy, and digital technologies.

The \$350 million Higher Education State Investment Fund is also underway. The Government is working with universities to identify projects that will support Victoria's innovation sector and create Victorian jobs. Several projects have already been funded and announced, including the University of Melbourne and Illumina Genomics Hub which will bring together the best of genomic expertise and technology in Australia.

The Government has also established Apprenticeships Victoria to connect the future pipeline of apprentices with Big Build projects and support 1 500 opportunities each year to work on some of our biggest projects, including the new Footscray Hospital and North East Link.

## **Education and training for all Victorians**

The *2021-22 Budget* continues to solidify Victoria as the Education State. This starts with the early years, and this budget invests \$401 million in ensuring all Victorian children can access high quality early childhood education in the years before school. This includes \$167 million to continue the historic roll out of universal kindergarten for three-year-old children, reaching all Victorian families in 2022 and progressively increasing to a full 15-hour program per child in 2029.

For schools, the Education State means building a system that provides every student with the opportunity to thrive. A new School Mental Health Fund forms the centrepiece of a \$277 million package of measures to support student health, mental health and wellbeing in schools. The Fund will enable schools to select and implement mental health and wellbeing programs from an evidence-based menu that meet the needs of their students, while also connecting with specialist services where required. An additional \$70 million is provided to ensure children with disability and additional needs can access inclusive education.

Funding is also provided to continue and expand school programs, ensuring schools continue to provide a safe and modern education. This includes \$55 million to continue and increase funding for swimming and water safety programs in schools across Victoria, and \$39 million to improve outcomes for Aboriginal children. An additional \$1.6 billion is provided to deliver schools infrastructure, including 13 new and 52 upgraded schools and new investment in essential maintenance.

Teachers remain at the centre of a system that produces excellence, and the *2021-22 Budget* includes \$185 million for initiatives to support the education workforce. This includes \$148 million to establish the Victorian Academy of Teaching and Leadership, dedicated to the professional learning and development of Victorian teachers. Funding is also provided to deliver expanded supports to reduce the administrative burden on principals, allowing them to focus on leading teaching and learning.

Victoria's TAFE and training sector is at the centre of the Government's Jobs Plan, and this budget continues to invest to ensure that Victorians can access high quality, relevant training that gives them the skills we need for recovery. This includes investment of \$89 million in additional training places to meet demand, \$99 million in increased government contributions for subsidised training, and investment in system reform (see Box 1.3). Funding is also provided to improve access to pre-accredited digital literacy and employability skills training and to equip TAFEs with the tools they need to provide modern traineeships and apprenticeships.

### **Box 1.3: Skills for Victoria's Growing Economy**

The Government commissioned the *Skills for Victoria's Growing Economy* review, chaired by Jenny Macklin, into Victoria's post-secondary education and training system. The final report, released in February 2021, made several recommendations for improving Victoria's skills and training system so it can deliver the skills Victoria needs now and into the future.

The *2021-22 Budget* begins the process of implementing a new vision for the training sector, guided by the recommendations of this review. At the centre of this vision is an investment of \$86 million to establish the Victorian Skills Authority.

The Victorian Skills Authority will be an anchor organisation, bringing together industry, providers and other stakeholders to identify priority training areas and develop an annual Victorian Skills Plan. The Victorian Skills Authority will also support continuous improvement in the quality of teaching and training across the system.

Funding is also provided to establish the Office of TAFE Coordination and Delivery as a separate business unit in the Department of Education and Training by mid-2021. This office will lead public provider strategy and collaboration across TAFEs, ensuring the TAFE network remains well placed to respond to Government priorities.

## Strong and safe communities

The Government is investing in fire services across the State, continuing Safer Together, Victoria's approach to reducing bushfire risk, and responding to recommendations from the Inspector-General for Emergency Management Inquiry into the 2019-20 Victorian Fire Season. This budget provides \$384 million for a range of initiatives to reduce the impact of bushfires on Victorian communities and the environment, including enhancing Forest Fire Management capability, increasing mechanical fuel treatments, and maintaining planned burning. Safety equipment will be improved and assets that support fire access and response will also be upgraded.

Dedicated funding will see the Victorian Traditional Owner Cultural Fire Strategy implemented, supporting Traditional Owners to undertake cultural burning and ensure this knowledge is sustained through generations.

The Government continues to advance treaty, progress Aboriginal self-determination and improve outcomes of Aboriginal Victorians. This budget provides a record investment of \$448 million to continue this work, including \$116 million to provide culturally safe care and support the mental health and wellbeing of Aboriginal Victorians. Funding of \$58 million is provided to establish the Yoo-rook Justice Commission in Victoria and to support the First People's Assembly of Victoria to establish a formal truth-telling process with Aboriginal Victorians to recognise historic wrongs and address ongoing injustices.

This budget continues to support vulnerable children to stay safe and help families stay together when possible. Funding of \$1.2 billion is provided for child protection and family services initiatives. This includes an expansion of the child protection workforce and a trial of a new whole-of-family support model for families with multiple health, justice or human services needs to divert them from acute and tertiary service usage.

An additional \$354 million is provided to support victim survivors and address family violence. This includes support for enhanced family violence information sharing and risk assessment, establishing specialist family violence courts, responding to demand for sexual assault services in adults and young people and delivery of specialist interventions targeted at perpetrators.

This budget provides funding of \$194 million for a package of measures to support people who are homeless and at-risk of homelessness. This includes the Private Rental Assistance Program to support more than 7 000 households annually to establish or maintain a private rental tenancy, an expansion of housing supports for people exiting prisons and continued assertive outreach for rough sleepers.

Vulnerable young people will be supported through a \$25 million package, including community-led initiatives providing culturally specific early interventions for at-risk cohorts, the Regional Presence Project to strengthen engagement between young people and their community and the Marram Nganyin Aboriginal Youth Mentoring Program.

This budget also provides support for LGBTIQ+ Victorians, including funding for Melbourne Pride 2021, a major one-off event to mark the 40-year anniversary of the decriminalisation of homosexuality by the Victorian Parliament and for the continuation of the LGBTIQ+ organisation grants program and the LGBTIQ+ Leadership Program.

Funding of \$210 million is provided to help address court backlogs caused by the COVID-19 public health restrictions, delivering new magistrates and judges, court staff, online services, support for judges and additional resources across the justice system. Victorian integrity agencies will also receive increased funding (see Box 1.4).

#### **Box 1.4: Boosting funding for integrity agencies**

The Government recognises the importance of properly funding integrity agencies to support accountability and ensure public sector integrity is upheld.

The *2021-22 Budget* provides the Independent Broad-based Anti-corruption Commission (IBAC) with an additional \$14 million to continue to support its ability to investigate and prevent corruption and misconduct, and implement recommendations from the Royal Commission into the Management of Police Informants<sup>(a)</sup>.

This includes funding to uplift its technology to enable its staff to work securely and effectively from any location. IBAC will also be independently audited to ensure it is meeting its objectives effectively, economically, and efficiently.

The Victorian Ombudsman is also provided with an additional \$11 million to continue to meet its legislative requirements, support its transition to budget independence and meet cost pressures associated with its operations.

While there are differing scopes and remits of these bodies across jurisdictions, funding for these agencies in Victoria in proportion to the public sector workforces they monitor and hold to account is above the average of other Australian states.

- The funding boost to IBAC will provide funding equivalent to \$199 per Victorian public servant in 2021-22 compared to \$81 per public servant for the New South Wales equivalent agency while undertaking a similar number of investigations in 2019-20; and
- The Ombudsman's funding will be boosted to a level equivalent to \$75.70 per Victorian public servant in 2021-22. This is higher than New South Wales, which provided its equivalent agency with \$73.32 per public servant in 2019-20.

*Note:*

*(a) A Treasurer's Advance of \$7 million in 2021-22 will also be approved for urgent additional investigative, prevention, review and communications activities*

## Keeping Victorians connected

The *2021-22 Budget* builds on the Government's record investment in Victoria's transport infrastructure and services to improve travel times, safety, accessibility and support jobs across the transport sector.

This budget provides \$3.2 billion for public transport services and infrastructure, including \$986 million to build 25 brand-new, modern trains in Victoria and upgrade the Craigieburn Train Maintenance facility, increasing service capacity and supporting local jobs.

Funding of \$265 million is provided to plan for, upgrade and maintain suburban, regional and rural roads. This includes \$42 million to improve accessibility and productivity of the road network for freight. An additional \$386 million is provided for a new Road Safety Strategy to develop new safety technologies, deliver infrastructure upgrades, and other improvements helping to keep Victorians safe.

The Government recognises the importance of reducing emissions for the environment and the health of Victorians, and more than 25 per cent of all emissions in our State come from the transport sector. The Government has set a target of 50 per cent of all new light vehicle sales being zero emission vehicles by 2030. This budget funds \$46 million for Australia's first public Zero Emissions Vehicle Subsidy Program, \$15 million to add 400 zero emission vehicles to the Victorian government fleet and upgrade infrastructure across government owned and leased buildings, and \$5 million to establish an innovation fund for the commercial sector. In addition, \$21 million is provided to improve the safety and usability of Victoria's walking and cycling network.



## CHAPTER 2 – ECONOMIC CONTEXT

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- The Victorian economy is recovering rapidly from the economic shock in 2020 caused by the coronavirus (COVID-19) pandemic. Economic activity rebounded strongly in the December quarter 2020, and there are strong signs that this momentum has carried through into 2021.
- Employment has recovered to pre-coronavirus (COVID-19) levels, and Victoria’s employment recovery has broadly caught up to the rest of Australia.
- The economic recovery is expected to continue over the coming year. Business and consumer confidence are elevated, household balance sheets are strong in aggregate, interest rates are low, and government assistance is supporting economic activity and jobs. The Government’s pipeline of infrastructure projects will continue to underpin high levels of public investment.
- The roll-out of COVID-19 vaccines, globally and domestically, should further boost confidence and activity, especially when national borders reopen.
- Victoria’s economy is forecast to grow by 6.5 per cent in 2021-22, after an estimated fall of 2.0 per cent in 2020-21. The unemployment rate appears to have peaked, and is forecast to decline to an average level of 5.75 per cent in 2021-22, from 6.5 per cent in 2020-21.
- Beyond 2021-22, economic and employment growth are expected to return to more normal rates of growth, while the unemployment rate continues to decline.
- Risks to Victoria’s economic outlook remain greater than normal and continue to be dominated by the coronavirus (COVID-19) pandemic, including risks related to the global roll-out of vaccines, and further policy responses to support ongoing global and domestic economic recoveries.

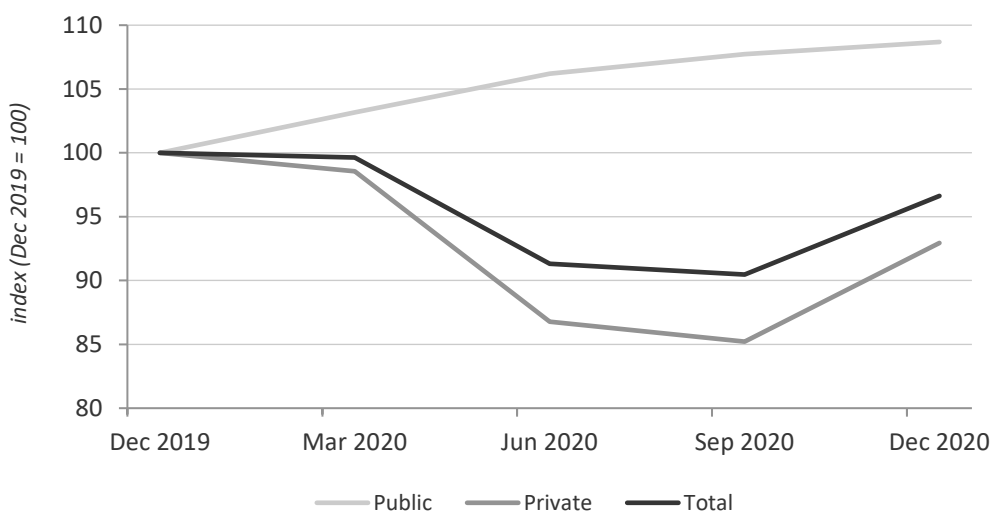
## VICTORIAN ECONOMIC CONDITIONS AND OUTLOOK

Following the release of the *Jobs Plan* as part of the *2020-2021 Budget*, the Victorian economy is recovering rapidly from the economic impacts of the coronavirus (COVID-19) pandemic. The easing of most domestic public health restrictions and elevated levels of government and monetary support are boosting activity and confidence. The economic recovery is expected to continue over the coming year, which will help further reduce spare capacity in the economy. Against this backdrop, however, national borders remain largely closed and there continues to be a need for some public health restrictions to remain in place. This will continue to disproportionately affect some sectors of the economy, such as international education and tourism.

Economic growth averaged 3.3 per cent and employment growth averaged 3.1 per cent a year over the five years to 2018-19, the strongest growth of all the states. However, economic activity and employment fell sharply from early 2020, as governments across Australia imposed restrictions on economic and social activities to limit the spread of COVID-19. Further public health restrictions were implemented in Victoria from July 2020, to save lives and enable sustainable economic recovery.

The Victorian economy rebounded strongly in the December quarter 2020 as public health restrictions were progressively eased. The rebound was led by consumer spending as consumer-facing businesses reopened, and business investment and dwelling construction also increased. In total, private demand rose by more than 9 per cent in the December quarter, although it remains well below pre-coronavirus (COVID-19) levels. By contrast, public demand has risen strongly to be well above where it was in early 2020, which has helped cushion the effect of the coronavirus (COVID-19) pandemic on the economy (see Chart 2.1).

**Chart 2.1: State final demand, public and private sectors <sup>(a)</sup>**



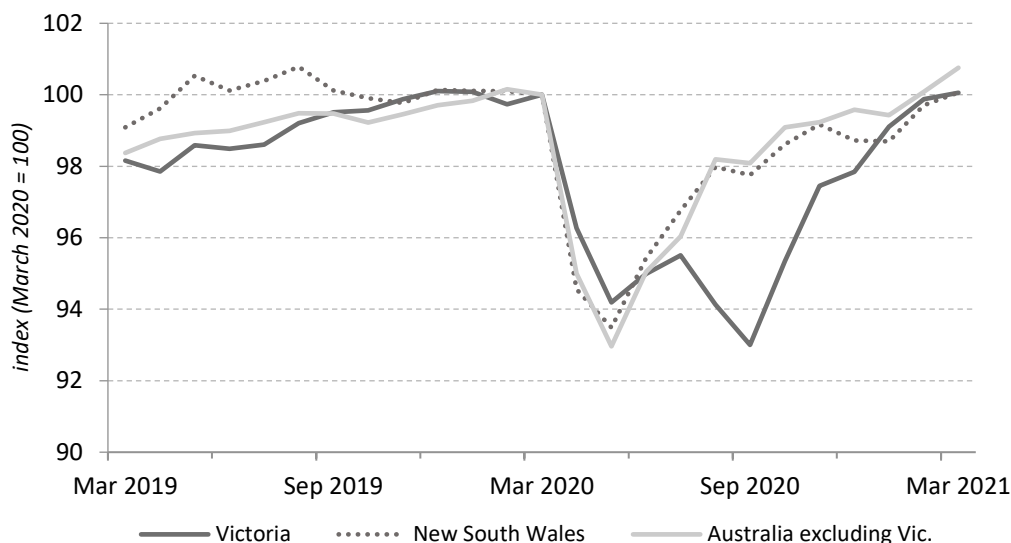
Source: Australian Bureau of Statistics

Note:

(a) Private final demand is the sum of consumer spending, business investment, dwelling investment and ownership transfer costs. Public demand is the sum of State/local and Commonwealth government consumption spending and investment.

Overall, Victoria’s gross state product (GSP) is forecast to have contracted by 2.0 per cent in 2020-21. Despite a longer period of necessary public health restrictions in Victoria in 2020, by early 2021 Victoria had broadly caught up to the national economy on many key economic indicators, including employment (see Chart 2.2).

**Chart 2.2: Employment, Victoria and rest of Australia**



Source: Australian Bureau of Statistics

Victoria’s economic recovery is expected to continue over the coming year. Business and consumer confidence are elevated, households overall have accumulated additional savings and monetary policy remains highly supportive. Global growth is also expected to rebound quite strongly in 2021, supported in part by very sizeable fiscal stimulus in the United States. The end of some Commonwealth economic supports – most notably the JobKeeper wage subsidy, which ended in late March this year – may lead to some disruption to employment and activity in the short term.

Victoria’s GSP is forecast to grow by 6.5 per cent in 2021-22, with the economy expected to return to its pre-coronavirus (COVID-19) size by late 2021. Employment is expected to rise by 2.5 per cent in 2021-22, while the unemployment rate will likely edge lower in the year, after an expected moderate increase in late 2020-21 due to the end of JobKeeper.

However, some constraints on the recovery will remain. Restrictions on international travel will constrain service exports, including education and tourism, into 2022 and drive continued very low population growth.

Over the longer term, the current period of low population growth will have an enduring effect on the size of the Victorian economy. Population growth has been an important driver of Victorian and national economic growth in recent years, led by high levels of net overseas migration. In the June and September 2020 quarters, Victoria recorded a net outflow of overseas migration, and net migration is expected to remain subdued for some time. This will leave the size of the Victorian population lower over the forecast period than would otherwise have been expected in the absence of the coronavirus (COVID-19) pandemic.

Table 2.1 sets out the economic forecasts for the *2021-22 Budget*, while Box 2.1 gives details of the major assumptions underpinning the forecasts. Given the current difficulty in interpreting annual figures, due to the large fluctuations in economic activity through 2020, Box 2.2 outlines the quarterly profile underlying these GSP growth rates. The nature of the coronavirus (COVID-19) pandemic means that the economic forecasts are subject to a higher degree of uncertainty than usual. Key risks to the outlook are discussed later in this chapter.

**Table 2.1: Victorian economic forecasts <sup>(a)</sup>** (per cent)

	2019-20 <i>actual</i>	2020-21 <i>forecast</i>	2021-22 <i>forecast</i>	2022-23 <i>forecast</i>	2023-24 <i>projection</i>	2024-25 <i>projection</i>
Real gross state product	(0.5)	(2.00)	6.50	3.25	2.75	2.75
Employment	1.2	(1.00)	2.50	1.25	1.75	1.75
Unemployment rate <sup>(b)</sup>	5.4	6.50	5.75	5.50	5.25	5.25
Consumer price index <sup>(c)</sup>	1.7	1.50	1.50	1.75	2.00	2.25
Wage price index <sup>(d)</sup>	2.4	1.25	1.75	2.00	2.25	2.50
Population <sup>(e)</sup>	1.5	0.00	0.30	1.20	1.70	1.70

Sources: Australian Bureau of Statistics; Department of Treasury and Finance

Notes:

(a) Percentage change in year average terms compared with the previous year, except for the unemployment rate (see Note (b)) and population (see note (e)). Forecasts are rounded to the nearest 0.25 percentage points, except for population (see Note (e)). The key assumptions underlying the economic forecasts include interest rates that broadly follow market expectations; an Australian dollar trade-weighted index of 61.5; and oil prices that follow the path suggested by oil futures.

(b) Year average.

(c) Melbourne consumer price index.

(d) Wage price index, Victoria (based on total hourly rates of pay, excluding bonuses).

(e) Percentage change over the year to 30 June. Forecasts are rounded to the nearest 0.1 percentage point.

### Box 2.1: Key forecast assumptions

The economic forecasts presented in this chapter depend on underlying assumptions about the roll-out of COVID-19 vaccines and restrictions on international travel, among other factors. These key assumptions are outlined below. Other factors that may affect the forecasts are discussed in the risks section in this chapter.

- Migrant flows remaining low until mid-2022 before gradually picking up, with international students slowly returning from early 2022 and tourist numbers picking up throughout 2022 as further Safe Travel Zones emerge and international borders re-open.
- Any further onset of COVID-19, in Victoria and nationally, is contained and only results in localised, short-term restrictions.

## Box 2.2: Quarterly GSP forecast profile

The scale of the economic downturn, and subsequent rebound, can make it more difficult to interpret annual forecast growth rates than in more normal times. Reference to the level of GSP, and on a quarterly basis, can be more informative in this circumstance.

Chart 2.3 shows quarterly forecasts for the level of Victorian GSP, and the corresponding financial-year average levels and growth rates. This quarterly GSP profile leads to the annual growth rate forecasts for 2020-21 and 2021-22 shown earlier in Table 2.1.

Economic output contracted sharply in the June quarter 2020, and fell again in the September quarter as a second and tighter phase of necessary public health restrictions was imposed. As restrictions eased through the December quarter, activity rebounded strongly and rapidly as businesses resumed activity and confidence increased. Growth momentum appears to have continued into the March quarter, though not quite as strongly. Growth is forecast to moderate in the June quarter, after two quarters of strong growth and as businesses and consumers adapt to the end of JobKeeper and other policy supports.

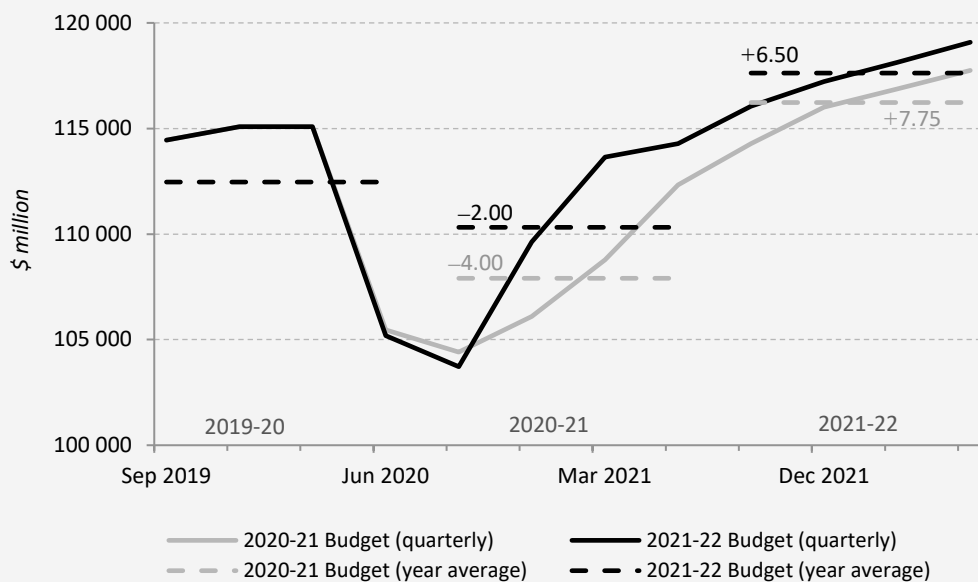
Victoria's economic recovery is expected to continue over 2021-22, which will help reduce spare capacity. However, the very strong growth that characterised the initial phase of recovery – largely due to the easing of public health restrictions amid significant government economic support – is expected to give way to more moderate increases in activity. It is estimated that GSP will return to pre-coronavirus (COVID-19) levels by about the September quarter 2021.

As shown in Chart 2.3, the initial recovery in Victorian output from the December quarter 2020 has occurred more quickly than was expected in the *2020-21 Budget*. This represents a pull-forward in the economic recovery, with the level of economic activity expected to return to pre-coronavirus (COVID-19) levels earlier than was previously forecast.

Given this pull-forward in the economic recovery, the level of GSP is expected to be higher in 2020-21 than was forecast in the *2020-21 Budget*, with about \$9.7 billion more economic activity forecast to occur in 2020-21.

The higher level of activity in 2020-21 means the forecast GSP growth rate for 2021-22 has been revised down, since the starting point is higher. Forecast GSP growth for 2021-22 remains very strong at 6.50 per cent, revised from 7.75 per cent in the *2020-21 Budget*. Importantly, the level of economic activity (GSP) in 2021-22 is expected to be about \$5.6 billion higher than was forecast in the *2020-21 Budget*.

**Chart 2.3: Quarterly real Victorian GSP levels, estimated actuals and forecast <sup>(a)</sup>**



Source: Department of Treasury and Finance

Note:

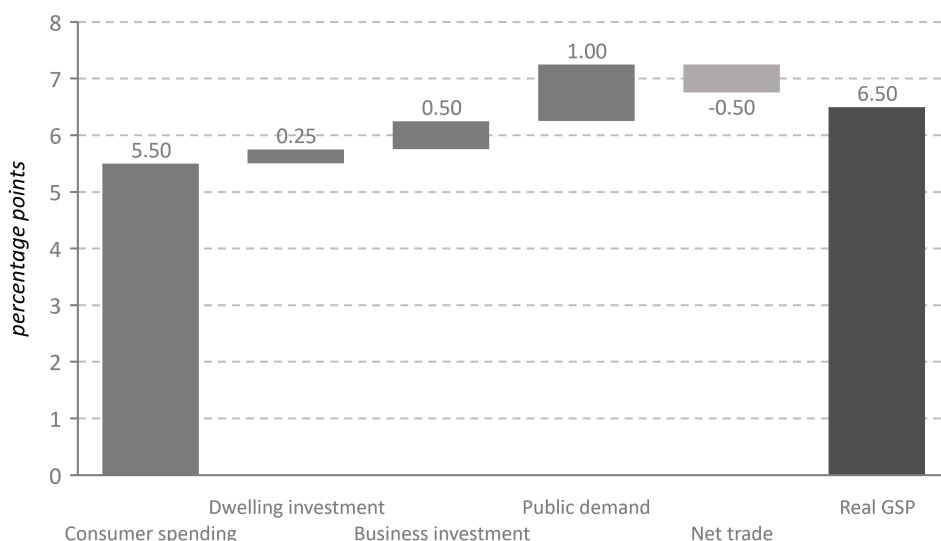
(a) Quarterly GSP estimates are derived by the Department of Treasury and Finance. The Australian Bureau of Statistics only publishes annual GSP estimates.

## Gross state product

Victorian GSP is forecast to increase by 6.5 per cent in 2021-22, following an estimated fall of 2.0 per cent in 2020-21 and a decline of 0.5 per cent in 2019-20. The strong headline result reflects an expectation that the recovery will continue over 2021-22, aided by the roll-out of vaccines and the further easing of restrictions, including the gradual return of international students from early 2022, government economic support and ongoing highly supportive monetary policy.

Economic growth is expected to be broad-based in 2021-22, with private sector activity rebounding, led by household consumption. This contrasts with 2020-21 when public demand is estimated to be the only positive contributor to growth in annual terms. All major components of GSP, with the exception of net trade, are forecast to contribute to growth in 2021-22 (see Chart 2.4).

**Chart 2.4: Forecast contributions to real 2021-22 GSP growth <sup>(a)</sup>**



Source: Department of Treasury and Finance

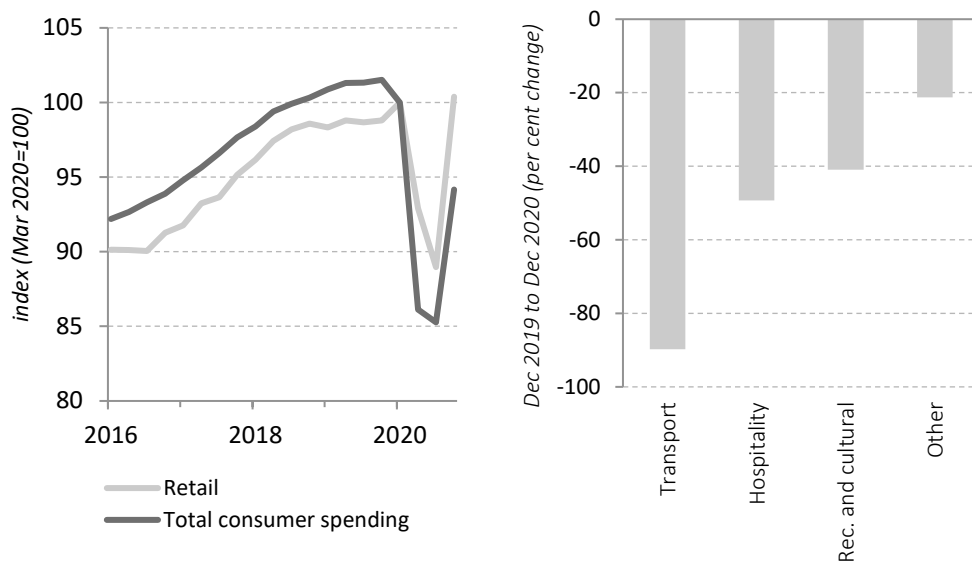
Note:

(a) Rounded to nearest 0.25 percentage points. Totals may not sum due to rounding.

Household consumption is forecast to make a large contribution to GSP growth in 2021-22. After falling in each of the first three quarters of 2020, consumer spending rebounded strongly in the December quarter as public health restrictions were progressively eased. By the end of 2020, Victorian retail sales were above pre-coronavirus (COVID-19) levels. Yet total consumer spending was still well below year-earlier levels as closed national borders, changes in consumer behaviour and residual public health restrictions continued to affect trading in some sectors – notably transport services, hospitality, and recreational and cultural services (see Chart 2.5).

In part, the strong growth in retail spending likely reflects some substitution towards goods from discretionary services and overseas travel. For example, spending on furnishings and household equipment, and goods for recreation, rose to record levels in 2020. Clothing sales also picked up strongly in the December quarter, while spending on passenger vehicles nearly doubled. An increase in online spending also supported growth in retail trade over the past year, as consumers adapted to public health trading restrictions.

**Chart 2.5: Consumer spending, retail and selected services (a)**



Source: Australian Bureau of Statistics

Note:

(a) Transport services; hotels, cafes and restaurants; recreational and cultural services; and other services (including hairdressers, beauty salons, drycleaners and domestic services). These services were 17 per cent of total spending in 2019, but only 10 per cent in 2020.

Over the coming year, spending is expected to be supported by continued improvement in the labour market, higher asset prices and ongoing elevated consumer confidence. Confidence may be further aided by the roll-out of vaccines. Strong income growth over the past year, driven largely by government payments – and coupled with constraints on some types of spending – led households to add to savings over 2020. Households are expected to draw down on some of these accumulated savings as confidence in the recovery grows. There has also been an improvement in household wealth, due to rising house prices and equity market values. Increased spending is expected on services in particular, assuming restrictions are eased further as the vaccine roll-out continues.

The outlook for household spending, though, remains more uncertain than usual. In the near term, the main uncertainty is how consumers have responded to the withdrawal of key policy supports in late March, notably JobKeeper and the JobSeeker Supplement, which occurred too recently to appear in the official economic data. It is likely that any dip in spending will be relatively short-lived as, along with strong aggregate household balance sheets, leading indicators of the labour market are positive. However, if the end of JobKeeper results in a larger disruption to the labour market, which then affects income growth and confidence in the recovery, the effect on household spending could be larger.

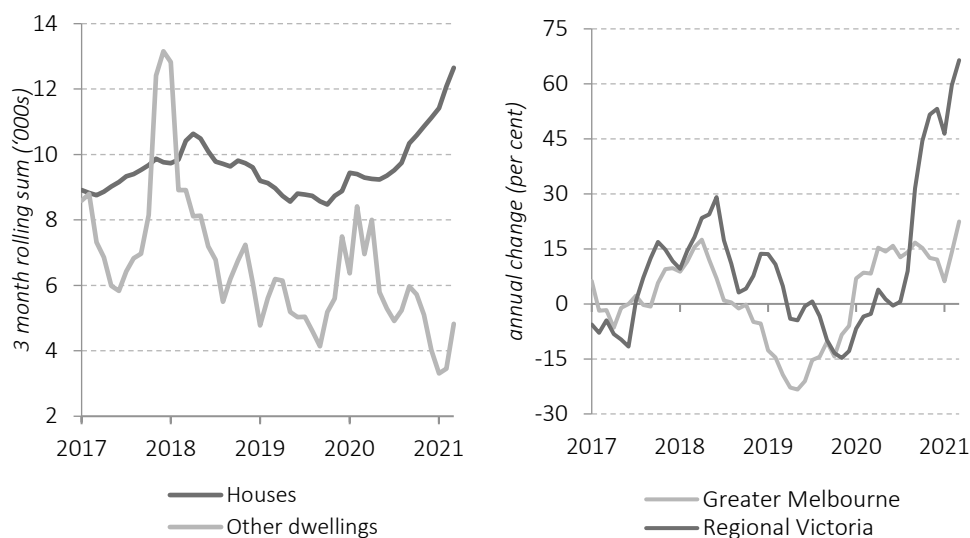


More generally, there is uncertainty about the extent to which households will draw on their accumulated savings. Rising household wealth and high levels of confidence could lead consumers to draw on their savings more quickly than expected, resulting in a larger increase in spending. Alternatively, households may remain considerably more risk-averse than they were before the coronavirus (COVID-19) pandemic, with households keeping a higher rate of precautionary savings than anticipated and spending less.

Dwelling investment is forecast to increase a little in 2021-22, following an expected moderate decline in 2020-21. Investment fell in the June and September 2020 quarters, largely reflecting earlier declines in house prices and building approvals which had reduced the construction pipeline. Workforce density restrictions also likely contributed to the decline in the September quarter. Construction rebounded in the December quarter, supported in part by the subsequent easing of these restrictions.

The outlook for construction is currently being supported by government incentives to build and renovate dwellings, and very low interest rates that are contributing to rising house prices (see Budget Paper No. 5, Chapter 4 *State Revenue* for a discussion on house prices). These conditions have contributed to a surge in approvals to build detached houses, with growth in house approvals particularly strong in regional Victoria (see Chart 2.6). By contrast, approvals for apartments and other attached dwellings have fallen sharply over the past year. This likely reflects the impact of closed national borders, with the absence of tourists and students weighing on the apartment market, particularly in inner Melbourne where vacancy rates are high and rents have fallen.

**Chart 2.6: Number of residential building approvals, Victoria, and growth in house approvals by location <sup>(a)</sup>**



Source: Australian Bureau of Statistics; Department of Treasury and Finance

Note:

(a) Growth in the number of house approvals by location is based on 3-month average data.

Business investment was down substantially in the June and September quarters 2020, with uncertainty about the economic outlook weighing on firms' appetite to invest. Since September 2020, surveyed business conditions and confidence have improved to be above pre-coronavirus (COVID-19) levels. Investment increased in the December quarter, driven by spending on machinery and equipment. This mainly reflected the purchase of motor vehicles and agricultural equipment, and was likely supported by government investment incentives.

Business investment is forecast to increase significantly in 2021-22, reflecting a partial recovery from the large fall estimated for 2020-21. The longer-term outlook for business investment will be partly determined by how individuals and businesses adapt to structural changes following the coronavirus (COVID-19) pandemic. Investment in new non-residential building (such as offices, retail and industrial premises) had been a significant contributor to growth in business investment before the coronavirus (COVID-19) pandemic, and construction activity was at a record high in the March quarter 2020. Work yet to be done on existing projects remains elevated, but this mainly reflects pre-coronavirus (COVID-19) pandemic investment decisions. Approvals for new projects have fallen substantially since early 2020, and if changes to individuals' work and shopping patterns persist, it is likely that new projects will not fully replace existing projects when completed.

Public demand is expected to be the only positive contributor to Victoria's GSP growth in 2020-21, as support from the Victorian and Commonwealth governments cushions the economic impact of the pandemic. Public demand is forecast to make another strong contribution to GSP growth in 2021-22, reflecting ongoing high levels of spending by both the Victorian and Commonwealth governments to support economic recovery. The Victorian Government's pipeline of transport and social infrastructure projects will continue to underpin high levels of public investment.

Trade in services has been severely disrupted during the coronavirus (COVID-19) pandemic, with the closure of national borders constraining international student enrolments and curbing international tourism. Softer international economic conditions have also limited demand for Victoria's goods exports. Meanwhile, Victorian imports of goods recovered sharply in the second half of 2020 – driven by increased spending on consumer goods, and supported by a pickup in business investment on machinery and equipment. With exports down and goods imports higher, net trade is expected to detract from growth in 2020-21.

Net trade is forecast to also detract from growth in 2021-22 as the economic recovery gathers pace. Higher machinery and equipment investment and, to a lesser extent, purchases of consumer goods are expected to underpin another solid increase in goods imports. This is forecast to outweigh an increase in goods exports resulting from stronger international economic conditions. Meanwhile, a pickup in service imports is expected as further Safe Travel Zones emerge and international borders re-open, led by a rise in outbound international tourism.

Despite this, service imports are forecast to remain significantly below pre-coronavirus (COVID-19) levels in 2021-22. It is expected to take some time for international travel to return to normal levels; some pent-up domestic demand for international tourism will likely be offset by a more cautious approach by other potential tourists, while many businesses and workers that have had to curb business travel may not consider it necessary to revert to pre-coronavirus (COVID-19) travel patterns. Service exports are also forecast to increase with the resumption of international education and inbound tourism; similarly, this is expected to take some time to return to pre-coronavirus (COVID-19) levels.

## OTHER ECONOMIC INDICATORS

### The labour market

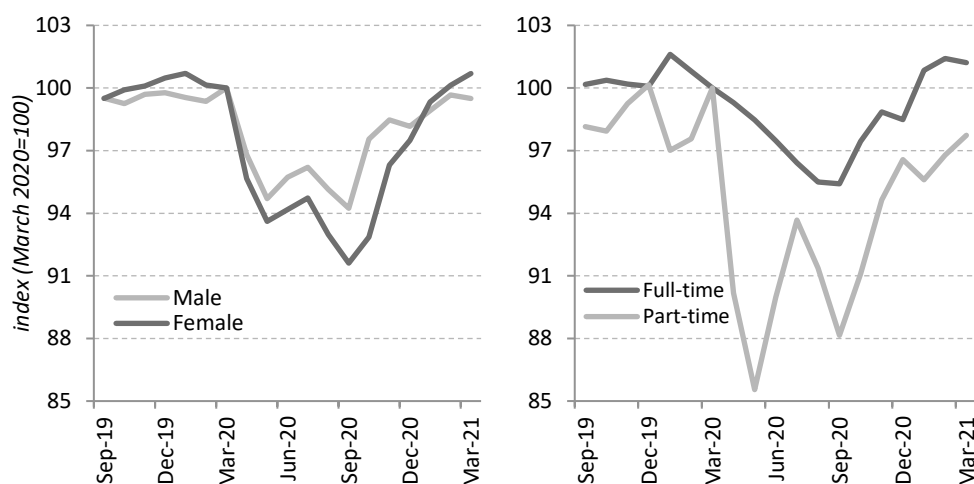
Victoria's labour market recovery has been rapid and strong. Employment and labour force participation, following large declines during 2020, have already returned to pre-coronavirus (COVID-19) levels, and the unemployment rate has likely already peaked. Female employment, which fell more sharply than male employment in 2020, has recovered strongly to be above pre-coronavirus (COVID-19) levels and has recovered further, in relative terms, than male employment. Nevertheless, there have been differences in the speed and extent of recovery in employment experienced to date across age groups, industries and regions. Further, the near-term employment outlook is subject to a higher degree of uncertainty than usual due to the recent end of the JobKeeper wage subsidy program in late March.

Employment rebounded strongly in the December quarter as public health restrictions were progressively eased, and there were further gains in the March quarter. Overall, employment rose by 243 000 persons between September 2020 and March 2021.

The employment recovery to March has been considerably faster than the recovery in economic activity, which remains below pre-coronavirus (COVID-19) levels. This difference largely reflects that average hours worked per worker remains lower than at the beginning of 2020, with total hours worked across the economy still below pre-coronavirus (COVID-19) levels.

Women and young workers are more likely to work in industries that have been most affected during the coronavirus (COVID-19) pandemic, such as accommodation and food services (see Box 2.3). Women were also more likely to take on caring responsibilities in 2020 during remote learning. Female employment has nevertheless recovered strongly to now be relatively higher than male employment, compared to March 2020 levels (see Chart 2.7), despite falling by more than male employment in 2020.

**Chart 2.7: Employment, by gender and full-time/part-time**



Source: Australian Bureau of Statistics

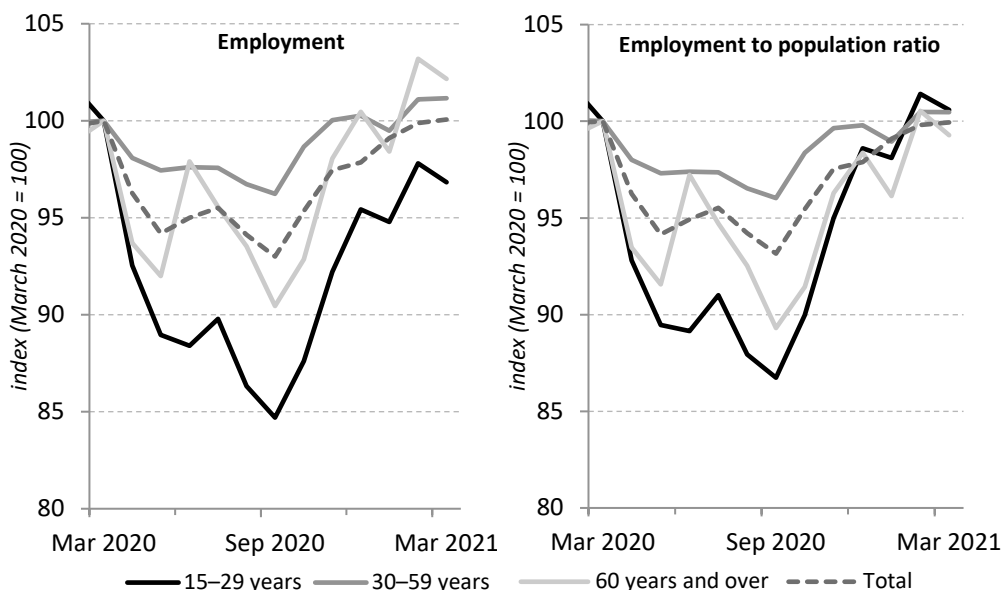
Victorian full-time employment is back above pre-coronavirus (COVID-19) levels but part-time employment continues to lag. Some customer-facing industries, such as accommodation and food services, and arts and recreation, are still affected by some restrictions, including border closures, and employment in these industries has lagged the broader recovery (see Box 2.3). These customer-facing industries have a much larger share of part-time and short-term casual positions. The JobKeeper wage subsidy was therefore less effective in protecting employment in these industries, as it excluded casual employees who had been with their employer for less than 12 months as at 1 July 2020.

Young people were also disproportionately affected by employment losses in 2020, with employment among those aged 15 to 29 years falling by over 15 per cent between March and September. Employment for young people initially rose sharply after the lifting of Victoria’s second phase of public health restrictions. The proportion of young people in employment has now recovered to around pre-coronavirus (COVID-19) levels (see the employment to population ratio in Chart 2.8).

However, there has been a net departure of young people since March 2020, partly as some current international students left Australia after finishing their courses, while few new international students arrived or returned due to closed national borders. This development has limited the total number of young people who have returned to employment, and is discussed later in the chapter (see *Population* below).

Older workers aged 60 years and over also experienced significant job losses, although employment has now surpassed March 2020 levels. Employment in some age groups was relatively unchanged through 2020, with employment among those aged 30 to 59 years falling by around 4 per cent and returning to March 2020 levels by November.

**Chart 2.8: Employment, and employment to population ratio, by age group <sup>(a)</sup>**



Source: Australian Bureau of Statistics; Department of Treasury and Finance

Note:

(a) Data for age groups are in original terms; total is in seasonally adjusted terms

### **Box 2.3: Employment by industry during the coronavirus (COVID-19) pandemic**

The employment effects during the coronavirus (COVID-19) pandemic have varied widely by industry. Differences were pronounced during 2020 when most public health restrictions were in place, and the Government responded with support to the most affected sectors in the *2020-21 Budget*, including through the Business Support Fund and additional industry-specific support to the tourism, hospitality and creative sectors. With the economy now in the early stages of recovery, some significant differences remain (see Chart 2.9).

Hospitality, tourism and other customer-facing industries were particularly affected during 2020, due to public health restrictions on in-person activity, border closures, and caution among consumers. Significant job losses occurred in hospitality and arts and recreation services between February and August 2020. Employment in the hospitality industry – which employs a high share of women and young people – declined by 70 300 persons (32 per cent) between February and August, accounting for 30 per cent of the total decline in Victorian employment over the period.

Large job losses also occurred in administrative and support services (which includes labour hire firms, travel agencies and tour arrangement services). Hospitality, arts and recreation and administrative and support services also have a relatively large share of casual workers, and this flexibility likely added to the number of job losses, especially with casual workers of less than one year having been ineligible for JobKeeper wage subsidies. Retail employment declined moderately, but was supported by a significant shift by consumers to online retailing, and a pickup in demand for household goods while people spent more time at home.

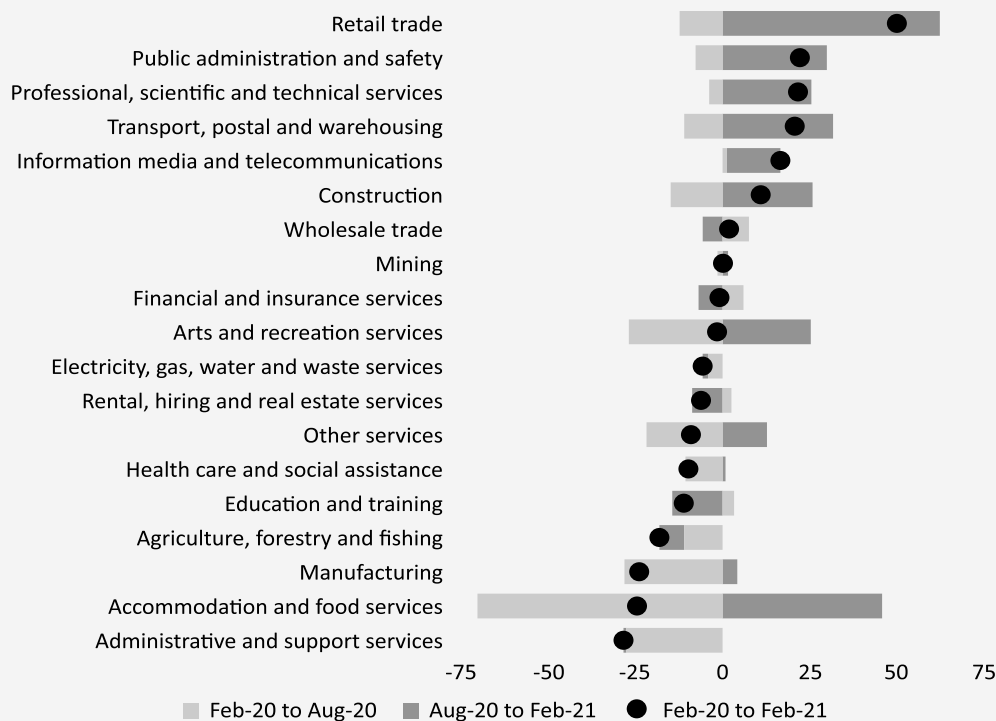
A number of other industries that were more easily able to adapt to remote working – such as professional services, finance and utilities – were less heavily affected by restrictions limiting in-person activity. These industries therefore experienced fewer job losses, and even employment increases in some cases.

By early 2021, many sectors had experienced an improvement in employment, following the gradual easing of public health restrictions and the pickup in economic activity. In several sectors that were less affected during 2020, employment is now considerably above pre-coronavirus (COVID-19) levels, while in others employment has been broadly stable. Employment in arts and recreation, which declined significantly in 2020, has largely recovered, aided by the resumption of sporting events and the reopening of gyms.

Employment in industries that rely on tourism and international students, though – such as hospitality, travel agencies (which are part of the administrative services industry) and education – remains relatively weak. These sectors remain constrained by the closure of national borders.

Employment in manufacturing fell sharply when the second phase of public health restrictions were introduced, amid weaker conditions in the sector. While conditions have since improved, employment in manufacturing is yet to recover. Agricultural, forestry and fishing employment also remains below what it was in early 2020.

**Chart 2.9: Cumulative change in employment by industry, '000 persons**

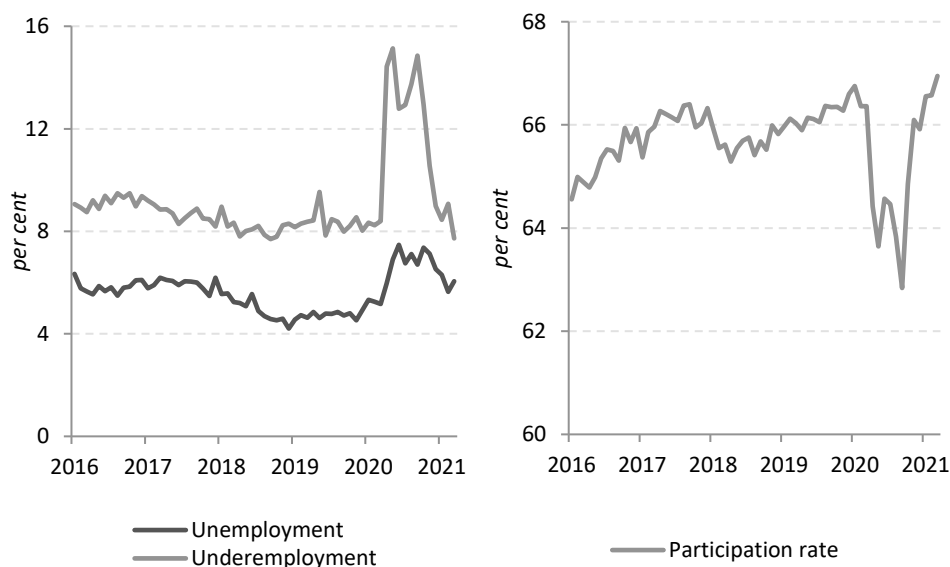


Source: Australian Bureau of Statistics; Department of Treasury and Finance

For 2020-21, employment is forecast to decline by 1.0 per cent in year-average terms. This reflects the low level of employment in the September quarter 2020 while public health restrictions were tightest, despite strong employment growth since restrictions were eased.

The strong recovery so far in aggregate employment has led to a fall in the unemployment rate, despite Victoria's workforce participation rate rebounding sharply to record-high levels. The unemployment rate was 6.1 per cent in March 2021, after peaking at 7.5 per cent in June 2020. Nevertheless, this remains above the March 2020 level of 5.2 per cent. The underemployment rate, which captures employed workers who would like to work more hours, has declined sharply from its peak to be around pre-coronavirus (COVID-19) and 2019 levels (see Chart 2.10).

**Chart 2.10: Unemployment, underemployment and participation rates**

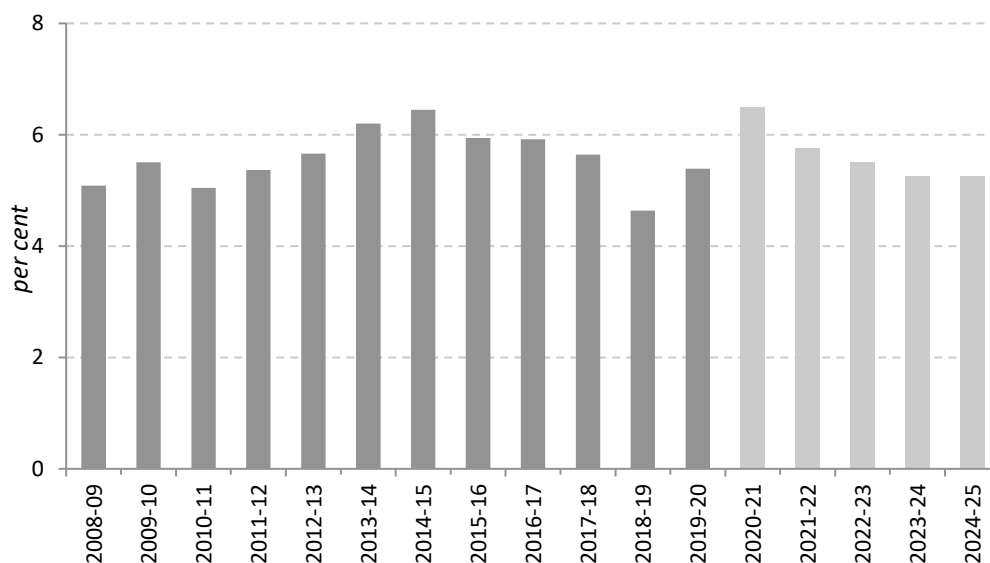


Source: Australian Bureau of Statistics

Employment growth is expected to be more subdued over the coming year, as the strong rebound following the easing of restrictions gives way to more steady rates of increase. Employment is forecast to rise by 2.5 per cent in 2021-22. The unemployment rate is forecast to average 5.75 per cent in 2021-22, down from an estimated 6.5 per cent in 2020-21 (see Chart 2.11).

The end of the JobKeeper program represents a short-term risk to the labour market. It is likely there will be a decline in employment, at least temporarily, in those industries still most affected by closed national borders. However, forward indicators of employment, such as job ads and business surveys, point to continued gains in employment more broadly across the economy. This suggests that these sectoral losses may be short-lived as employment opportunities are created elsewhere. Risks associated with the end of the JobKeeper program are also discussed later in the chapter (see *Risks to the Victorian Outlook* below).

**Chart 2.11: Unemployment rate, actual and forecast**



Source: Australian Bureau of Statistics, Department of Treasury and Finance

### **Box 2.4: Employment changes across Victoria's regions**

Employment conditions have varied significantly by region in Victoria during the coronavirus (COVID-19) pandemic. Metropolitan Melbourne and tourism-dependent areas of regional Victoria were particularly affected. The loss of international students and tourists particularly affected Melbourne, while tourism regions were also significantly affected by the closure of national borders. Longer and tighter public health restrictions in Melbourne, relative to regional Victoria, also contributed to greater employment losses in Melbourne during 2020.

To a large extent, variations in employment by region reflect the differing effects of the pandemic by industry (see Box 2.3).

Communities in regional tourism-reliant areas such as the Great Ocean Road, High Country, Geelong and the Bellarine, and Daylesford and Macedon Ranges have also been significantly affected, experiencing the largest percentage increases in JobSeeker recipients between March and December 2020 outside Melbourne. In some regions, these tourism losses followed the 2019-2020 Victorian bushfires. Tourism and hospitality spending in regional Victoria were also weighed down over July to November 2020 by restrictions preventing those in metropolitan Melbourne visiting regional areas.

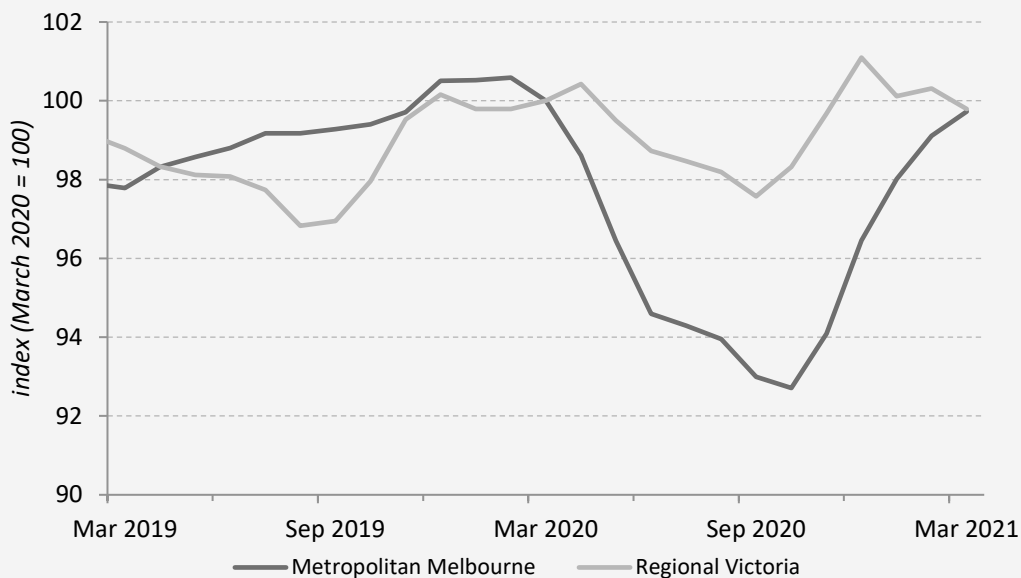
In inner Melbourne, alongside tourism, the closure of national borders has weighed on international student numbers. This has dampened demand for consumer goods and services, as well as rental accommodation. Further, customer-facing businesses in the central business district have experienced much lower customer demand, with a large proportion of office employees having worked remotely during most of 2020. By early 2021, the share of workers returning to central business district offices had risen but remained well below pre-coronavirus (COVID-19) levels.



Activity and employment in metropolitan Melbourne were, relative to regional Victoria, also affected by a longer period of public health restrictions to limit the spread of COVID-19 in the second half of 2020, and at their peak restrictions were tighter.

Employment in both regional Victoria and metropolitan Melbourne rebounded strongly with the easing of public health restrictions in late 2020. Overall employment in regional Victoria recovered more strongly than metropolitan Melbourne to be above pre-coronavirus (COVID-19) levels by late 2020. Conditions in regional Victoria have since eased somewhat, while employment in metropolitan Melbourne has continued to improve (see Chart 2.12). The unemployment rate for Melbourne, which increased substantially in early 2020, also remains considerably higher than that in regional Victoria (see Chart 2.13). This largely reflects that ongoing closed national borders continue to weigh on international tourists and student numbers.

**Chart 2.12: Employment, metropolitan Melbourne and regional Victoria <sup>(a)</sup>**

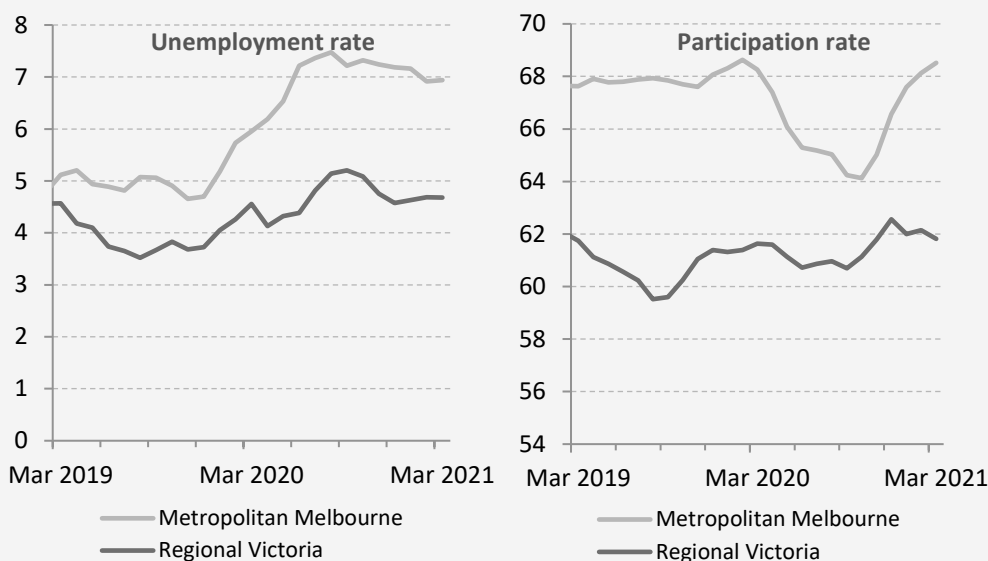


Source: Australian Bureau of Statistics; Department of Treasury and Finance

Note:

(a) Data are smoothed using a three-month moving average, and are not directly comparable to the total Victorian employment data cited above

**Chart 2.13: Selected labour market indicators by region, per cent <sup>(a)</sup>**



Source: Australian Bureau of Statistics; Department of Treasury and Finance

Note:

(a) Data are smoothed using a three-month moving average

## Wages

Victorian wages growth had been subdued in recent years prior to the impacts of coronavirus (COVID-19), though generally a little ahead of the national average. This slowdown in wages growth was consistent with other Australian states and international jurisdictions.

Wage growth slowed further in 2020 as many businesses introduced wage freezes or temporary wage cuts. Overall Victorian wages fell by 0.1 per cent in the June quarter 2020, and increased by just 0.2 per cent in the September quarter. Wages then increased by 0.7 per cent in the December quarter, although this increase was driven by the partial unwinding of earlier wage reductions, particularly in the professional and administrative services industries. For 2020 as a whole, wages rose by 1.7 per cent, the smallest calendar-year increase on record.

Business surveys indicate that wage pressures have picked up from recent lows, and this is consistent with findings by the Reserve Bank of Australia (RBA). In its May 2021 *Statement on Monetary Policy*, the RBA reported that more temporary wage cuts have been unwound since December, and fewer firms expect to have wage freezes in place in the coming months. Despite this, wage freezes remain fairly widespread across industries, with over a quarter of surveyed firms reporting to the RBA that a wage freeze was in place in April.

Wages growth is expected to be 1.75 per cent in 2021-22 and 2.0 per cent in 2022-23. As the economy recovers and spare capacity in the labour market is gradually reduced, wages growth is expected to increase moderately over the remainder of the forecast period from the current very low rates.

## Prices

Inflationary pressures remain subdued, although inflation has been somewhat volatile in recent quarters. This volatility reflects the unwinding of some temporary government support measures in the second half of 2020, such as free childcare, as well as a partial rebound in fuel prices over the same period after a large fall in the June quarter 2020. Housing rents are weak, with falls in the June and September quarters 2020 and only a slight rise in the following quarter. For 2020-21 as a whole, the Melbourne consumer price index (CPI) is forecast to rise by 1.50 per cent.

Looking ahead, inflation is expected to rise only gradually over the forecast period. This reflects the outlook for subdued wages growth for several years, as spare capacity in the labour market will take time to be absorbed. The appreciation of the Australian dollar since mid-2020 will put some downward pressure on inflation over the medium term. Further, inflation expectations remain well anchored.

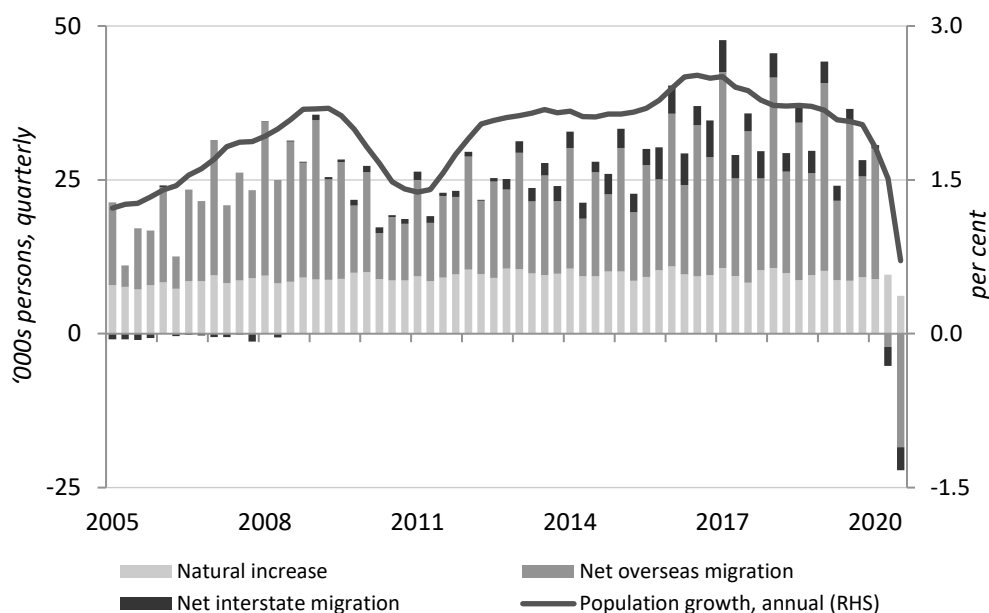
## Population

Victoria's population growth had been strong over the past decade, leading up to the coronavirus (COVID-19) pandemic. Annual population growth had been higher than in any other state or territory since 2013, reflecting Victoria's attractiveness as a place to live, work and study. The coronavirus (COVID-19) pandemic, though, has had a significant negative impact on population growth, with Victoria's population falling in outright terms in the September quarter 2020.

Net overseas migration had been the largest driver of Victoria's population growth for more than a decade. Australia's border closure, which came into effect in March 2020, led to negative net overseas migration in the June and September quarters as, amid some ongoing travel, more students and other foreigners living in Victoria returned home than expatriate Australians and migrants moved from overseas to Victoria (see Chart 2.14). The exit of international students and other younger workers from the State in 2020 has constrained the pickup in employment of young people. This is despite the broader economic and employment recovery that is now well underway, and the recovery in employment of young people as a proportion of the population.

The pattern of greater overseas departures than arrivals is expected to continue for at least the next year – although not to the degree observed in the September quarter, which coincided with Victoria's second phase of public health restrictions. Net interstate migration to Victoria had also been strong in recent years, although this too detracted from population growth in the June and September quarters.

**Chart 2.14: Change in Victoria’s population, total and by category**



Source: Australian Bureau of Statistics

Overall, Victoria’s population is forecast to be unchanged in 2020-21, before growing by 0.3 per cent over 2021-22. As national borders reopen, and confidence in the economic outlook improves, population growth is expected to slowly pick up, to reach around 1.7 per cent by 2023-24. Nevertheless, this remains below the average annual growth rate of 2.3 per cent over the five years before the coronavirus (COVID-19) pandemic.

## AUSTRALIAN ECONOMIC CONDITIONS AND OUTLOOK

The coronavirus (COVID-19) pandemic brought an end to Australia’s 28-year run of unbroken economic growth. Significant government support and success in limiting the spread of COVID-19 resulted in a much smaller negative economic impact and faster recovery than was initially predicted. After falling by a sharp 7.0 per cent in the June quarter 2020, the easing of public health restrictions in most states led to real gross domestic product (GDP) increasing by 3.4 per cent in the September quarter. It rose by a further 3.1 per cent in the December quarter, partly driven by the recovery commencing in Victoria at that time. Notwithstanding these strong results, output remained 1.1 per cent lower compared with the December quarter 2019.

As with Victoria, the large fall and subsequent rise in national consumer spending was the major contributor to fluctuations in GDP, with the largest ever fall in consumer spending in the June quarter, followed by large rises in the September and December quarters.

In its *2021-22 Budget* released in May 2021, the Commonwealth Government forecasts the Australian economy to grow by 4.25 per cent in 2021-22. This is expected to follow growth of 1.25 per cent in 2020-21, revised up significantly from a fall of 1.50 per cent expected in the Commonwealth's *2020-21 Budget* in October 2020. GDP is now estimated to have exceeded its pre-pandemic levels in the March quarter 2021.

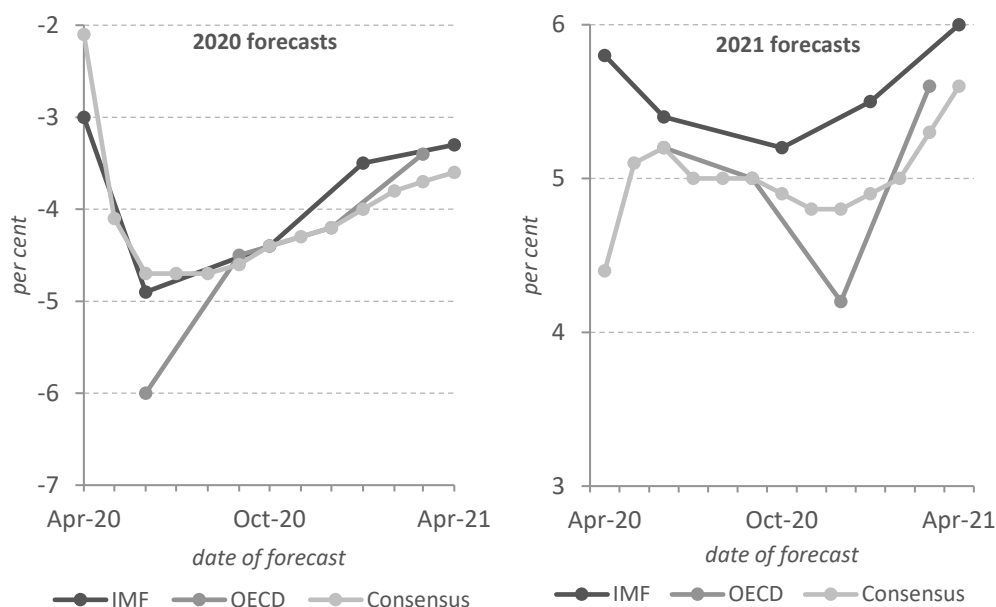
Household consumption and public demand are expected to be the main contributors to GDP growth in 2021-22. Business investment is expected to make a partial recovery. Dwelling investment is expected to stabilise in 2021-22 and then decline in 2022-23, following an expected rise in 2020-21 supported by government incentives, low interest rates and rising house prices. Net exports are forecast to detract from growth in 2021-22 and 2022-23, with outbound tourism expected to be larger than inbound tourism once international border restrictions ease, and with demand for imported goods expected to increase.

Employment losses in 2020 have been reversed and employment has reached a new high. This has driven the unemployment rate down from a peak of 7.5 per cent in July 2020 to 5.6 per cent in March 2021. The Commonwealth Government forecasts that the unemployment rate will continue to decline. With this fall, wages growth is expected to pick up gradually over the forecast period. Inflation is expected to strengthen from the second half of 2021 onwards, reflecting a reduction in labour market slack and expected wage growth, and headline inflation is expected to approach the Reserve Bank of Australia's 2 to 3 per cent target band in 2022-23.

## **INTERNATIONAL ECONOMIC CONDITIONS AND OUTLOOK**

Global economic output fell sharply in the first half of 2020 due to the public health restrictions and lower confidence in response to coronavirus (COVID-19). Economic recovery started in most major economies around mid-2020 as initial restrictions eased, although the renewed spread of COVID-19 in some countries stalled momentum in the December quarter. Still, economic data for late 2020 were better than previously expected. This, along with falling COVID-19 case numbers, the roll-out of vaccines, greater fiscal stimulus and highly supportive monetary policy settings have led to upgrades to global growth estimates for 2020 and forecasts for 2021 (see Chart 2.15).

**Chart 2.15: Global real GDP growth forecasts <sup>(a)</sup>**



Sources: IMF; OECD; Consensus Economics

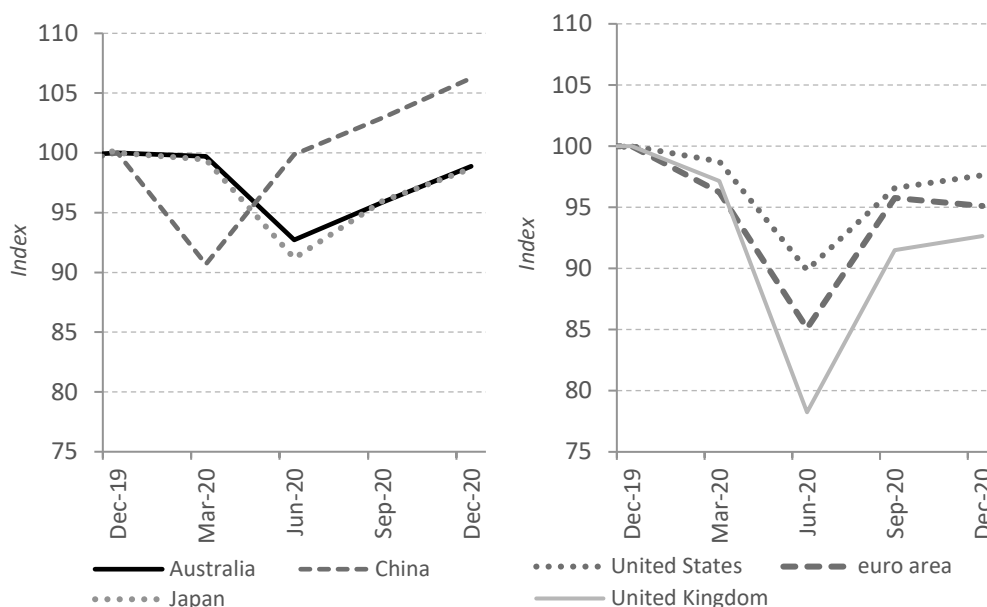
Note:

(a) In March 2020, the OECD forecast growth of +2.4 per cent in 2020 and +3.3 per cent in 2021 (not shown in charts).

In China, GDP fell sharply in the March quarter 2020, as large parts of the economy were shut down to limit the spread of COVID-19. Activity rebounded strongly in subsequent quarters, leading growth over the year to the December quarter to be 6.5 per cent, around the typical pre-coronavirus (COVID-19) growth rate for the Chinese economy.

In other major economies, the decline in GDP was largest in the June quarter, with the size of the decline varying according to the extent of the spread of COVID-19, the scale of containment measures and the policy response enacted (see Chart 2.16). Widespread relaxation of restrictions led to a strong rebound in the September quarter. Sustained recovery has been largely contingent on keeping COVID-19 cases contained, with outbreaks and the resultant re-introduction of public health restrictions limiting growth in the December quarter across multiple countries. In the March quarter 2021, significant restrictions continued across the United Kingdom and Germany and in parts of France and Italy, constraining economic activity. This came despite the vaccine roll-out in these countries having started in late 2020. Meanwhile, the significant fall in the number of people with COVID-19 and the accelerated roll-out of vaccines in the United States has led to loosening restrictions across multiple states there. The United States also passed a very large \$US1.9 trillion (9 per cent of United States GDP) stimulus package into legislation in March, which contained significant payments to households. The easing of restrictions and this stimulus should support a significant rebound in economic activity in the United States in 2021, as well as benefiting the United States' main trading partners.

**Chart 2.16: Real GDP index, December quarter 2019=100 <sup>(a)</sup>**



Source: Individual statistics agencies; Department of Treasury and Finance; Macrobond

Note:

(a) Chinese index is derived by DTF from quarterly seasonally adjusted growth rates

The International Monetary Fund (IMF) estimates that global GDP fell by 3.3 per cent in 2020, the largest fall in global output since the Great Depression. Despite the sharp fall, the IMF estimates that the contraction could have been around three times as large if not for the extraordinary policy responses around the world. The global economy is expected to rebound by 6.0 per cent in 2021, which would take the level of global output to around 2.5 per cent above 2019 levels (see Table 2.2).

This growth forecast for 2021 is nearly one full percentage point higher than was forecast last October, reflecting additional fiscal support in a few large economies (especially the United States) and the expected economic benefits in the second half of 2021 of the roll-out of vaccines. The pace of recovery also reflects continued adaptation of all sectors of the economy to the challenging health situation. The global recovery will vary significantly across countries, depending on the severity of the health crisis, the extent of domestic disruptions to activity, exposure to cross-border spill overs and the effectiveness of policy support to limit persistent damage.

The IMF’s forecasts assume that vaccines are broadly available across advanced economies and some emerging market economies in mid-2021, and across most countries by the second half of 2022. As discussed in the next section, the potential for a slower roll-out of vaccines due to production or distribution delays, and the potential for new COVID-19 variants that are resistant to available vaccines, is an important downside risk to the global and Victorian economic outlooks.

**Table 2.2: Summary of IMF's global economic forecasts <sup>(a)</sup> (per cent)**

	2019 actual	2020 estimate	2021 projection	2022 projection
<b>World output</b>	<b>2.8</b>	<b>-3.3</b>	<b>6.0</b>	<b>4.4</b>
<b>Advanced economies</b>	<b>1.6</b>	<b>-4.7</b>	<b>5.1</b>	<b>3.6</b>
United States	2.2	-3.5	6.4	3.5
Euro area	1.3	-6.6	4.4	3.8
Japan	0.3	-4.8	3.3	2.5
<b>Emerging market and developing economies</b>	<b>3.6</b>	<b>-2.2</b>	<b>6.7</b>	<b>5.0</b>
China	5.8	2.3	8.4	5.6
India	4.0	-8.0	12.5	6.9
<b>ASEAN-5 <sup>(b)</sup></b>	<b>4.8</b>	<b>-3.4</b>	<b>4.9</b>	<b>6.1</b>

Source: IMF, World Economic Outlook, April 2021

Notes:

(a) Not all countries or regions are listed in the table.

(b) ASEAN-5 economies are Indonesia, Malaysia, Philippines, Thailand and Vietnam.

## RISKS TO THE VICTORIAN OUTLOOK

Risks to Victoria's economic outlook remain greater than normal and the forecasts are subject to a high degree of uncertainty. These risks continue to be dominated by the coronavirus (COVID-19) pandemic, including risks around the domestic and global roll-out of vaccines, the efficacy of vaccines on emerging strains of COVID-19, and any further economic policy responses to support the ongoing recovery of the domestic and global economies.

On the upside, the ongoing recovery in consumer spending could be stronger than anticipated. Employment has returned to pre-coronavirus (COVID-19) levels, households have added to their savings, and consumer confidence is elevated. Household wealth has also risen: house prices have recovered their losses from 2020 and are at new highs, and equity markets have also rebounded. Combined, these factors could lead to consumer spending rising more strongly than expected over the coming year.

On the downside, however, there is a risk to consumer spending in the near term from the recent end of key policy supports. These include the JobKeeper program, the further decline in unemployment benefits, and banks' mortgage repayment deferrals. This could cause spending growth to weaken in the near term as some consumers adjust to changes in income. More generally, households may remain more risk-averse than they were before the COVID-19 pandemic, resulting in households keeping a higher rate of precautionary savings than anticipated and spending less.



The withdrawal of Commonwealth stimulus measures, in particular the end of the JobKeeper program, is a broader downside risk to the economy in the near term. It is likely there will be a decline in employment in those industries still most affected by closed national borders. These losses are likely to be short-lived in net terms as employment opportunities are created elsewhere. However, if the end of JobKeeper results in a larger disruption to the labour market, this would negatively affect income growth and confidence in the recovery more broadly, which would flow through to consumer spending.

A key downside risk is if there are any significant delays or problems with the global roll-out of COVID-19 vaccines. This would delay the timing of the national borders reopening. The longer national borders remain closed, the longer net overseas migration, and international education and tourism exports, will remain very low. The speed and efficacy of the roll-out of vaccines – including the efficacy of vaccines against any future COVID-19 variants – are also key risks to the global economic outlook. Appendix A *Sensitivity Analysis* presents analysis of the effects on the Victorian economy of a delay in the global roll-out of vaccines. In this scenario, the delay leads to the renewed spread of COVID-19 globally and reimposed public health restrictions, as well as a delay to the reopening of Australia's border.

The further spread of COVID-19 domestically, requiring the reintroduction of broad activity restrictions for extended periods, also presents a key downside risk, with this risk more material until the population is widely vaccinated. This would lead to renewed falls in consumer spending and employment.

Future levels of net overseas migration are a key uncertainty and pose a long-term risk to the economic outlook. It is assumed that migration levels, including temporary international student migrants, will start approaching pre-coronavirus (COVID-19) levels towards the end of the forecast period. If the recovery in net overseas migration occurs more slowly than expected, this would weigh on the longer-term economic outlook for the State.



## CHAPTER 3 – INVESTING EARLY FOR BETTER AND FAIRER OUTCOMES

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### Key points

- Victoria is investing in reforms that put people at the centre of service delivery – continuing the transformation of how the Government delivers services to people, with a shift towards early intervention and diversion.
- An early intervention approach informs major initiatives in this budget, including the Government’s response to the Royal Commission into Victoria’s Mental Health System.
- The budget’s investments in early intervention show the Government is focused on pursuing interventions that improve outcomes and avoid growing acute service usage.
- The Government is committed to gradually shifting the service system to provide more early interventions. To further this reform, the budget supports the further development of an Early Intervention Investment Framework.

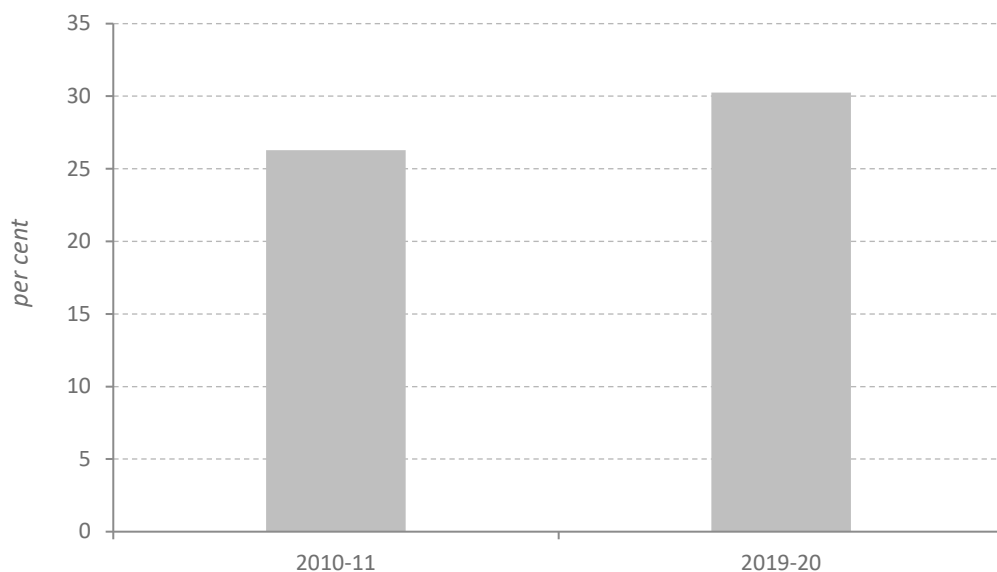
Victoria has led reform in changing the way governments provide key services such as family violence prevention and social housing – supporting these reforms with significant investments. This budget continues the Government’s social reform agenda, with a record investment of \$3.8 billion to expand and reform mental health services.

At the same time, the growth in demand for acute health and social services, has accounted for an increasing portion of the State’s expenses over the past decade (see Chart 3.1).

These are indispensable services for Victorians in need, and yet often they also indicate that people did not receive the help they first needed.

By providing help to our citizens earlier, before they enter crisis, we can most importantly serve Victorians better, while also reducing the pressure acute services place on the budget.

**Chart 3.1: Share of state government total expenses spent on acute government funded services, 2010 to 2020**



Source: 2010-11 Budget, 2019-20 Budget.

Note: Acute services are defined as Child Protection, Corrections, Youth Justice, Police, Housing, Acute Health and Mental Health.

### The benefits of early intervention

A large portion of the Government’s expenditure is directed to acute services. These are the vital services that provide relatively intensive assistance, such as hospital admissions, or respond to crises, such as ambulance transports, or are an option of last resort, such as jail or placement of children in out of home care.

Relative to spending on acute services, Government spending on prevention and early intervention programs remains low – although it has increased in recent years in areas such as family violence prevention and child and family services.

While acute services will always be an essential part of the service response, there is growing acknowledgement that more should be done earlier to address issues as they emerge, with such early interventions guided by a clear and growing evidence base.

A service system that is not appropriately balanced with adequate access to early intervention assistance can have severe consequences for individuals, including:

- problems becoming entrenched and requiring more intensive, intrusive and/or sustained intervention for the person than if they had been addressed earlier, such as family services providing parenting and counselling support at the first signs of vulnerability;
- escalation of problems that have flow on effects and result in compounding impacts. For example, persons of mental ill health are more vulnerable to risk factors such as alcohol and drug addictions, and unemployment. These factors in turn impact on people’s capacity to access and benefit from mental health services and increase the likelihood of homelessness; and

- intergenerational impacts on children emerging from unaddressed family issues. For example, children of families with persistent challenges such as drug and alcohol usage, homelessness or parenting difficulties are at greater risk of entering out-of-home-care, experiencing disrupted schooling and decreased educational attainment, and increasing the likelihood they interact with the justice system.

There are costs to the economy too. By not providing timely and effective assistance, people's ability to gain and maintain employment is affected, causing workforce participation and labour productivity to decline. These consequences mean that governments also incur increasing costs through greater usage of intensive acute services.

Targeted early interventions, provided by skilled professionals over a prolonged period, have been shown to be effective at addressing entrenched issues, improving outcomes for people, and reducing the need for acute services.

The Government is committed to gradually shifting the service system to provide more early interventions. Through this shift, the Government will further improve outcomes for Victorians and reduce funding pressures through avoided costs – freeing up funding capacity for other priorities.

This budget continues this commitment through the Government's response to the Royal Commission into Victoria's Mental Health System - a record investment of \$3.8 billion in mental health services with a focus on shifting to earlier interventions. The budget invests a further \$324 million in programs that begin to shift the system to one more focused on earlier interventions.

## **MENTAL HEALTH REFORM**

The Government's response to the Royal Commission into Victoria's Mental Health System emphasises holistic and community-based responses to support mental health and wellbeing.

### **The prevalence of mental illness**

All Victorians benefit from access to a compassionate and effective mental health system – one in five Victorians experiences mental illness each year, and almost every second Victorian will be affected by mental illness in their lifetime.

There is evidence the coronavirus (COVID-19) pandemic has exacerbated the prevalence of mental illness. The use of crisis and support organisations, such as Lifeline and Beyond Blue, increased by more than 20 per cent and 40 per cent respectively compared with before the pandemic.

## Problems in the current mental health and wellbeing system

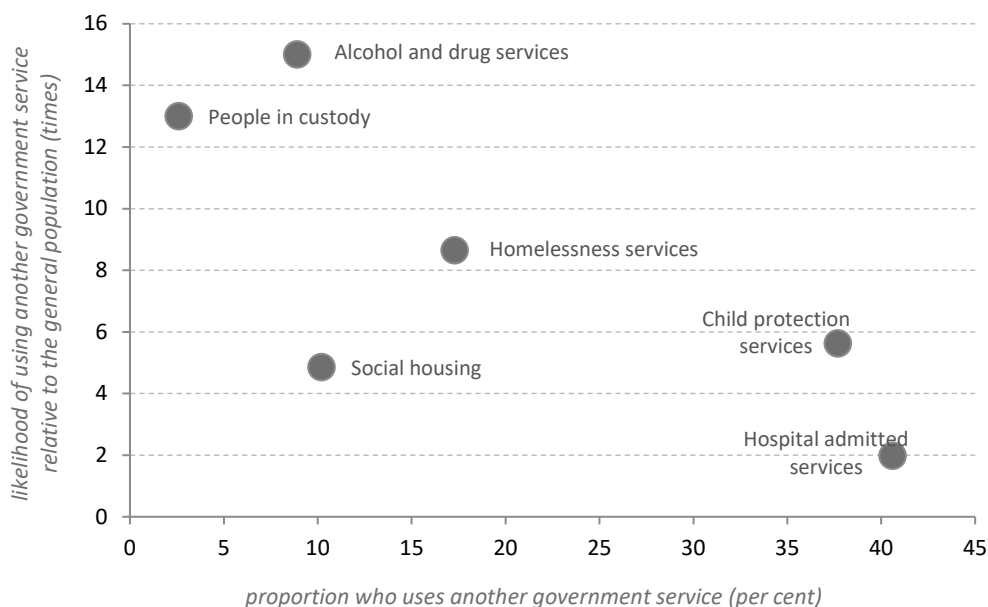
The Royal Commission into Victoria’s Mental Health System shone a light on structural gaps and failures in the system, and set out a roadmap to transform mental health and wellbeing services over the next decade.

Primary care and community-based services are not keeping up with demand, resulting in an over-reliance on acute services. In 2019-20, nearly half of all new referrals to clinical mental health services were from acute health and emergency departments.

Victorians accessing public specialist mental health services are often also users of other government services (Chart 3.2). Yet there is limited coordination and integration between services.

The Royal Commission into Victoria’s Mental Health System called for transformational reform, building a system of care and support that is inclusive, effective, and importantly accessible – investing in people before issues become urgent and entrenched in their lives.

**Chart 3.2: Victorians accessing public specialist mental health services using other Victorian Government services, 2017–18**



Sources: Royal Commission into Victoria’s Mental Health System, 2019, Interim Report, Figure 12.7

## The Government is stepping up to the challenge

The Government is committed to delivering reform, with the *2020-21 Budget* previously investing a record \$869 million to support the mental health system, including \$605 million to start implementing the recommendations of the Royal Commission into Victoria's Mental Health System.

As the next step in the Government's response to the Royal Commission into Victoria's Mental Health System, this budget invests a record investment of a further \$3.8 billion to improve mental health and wellbeing. In addition to equipping the system to meet acute demand and prevent suicide, the budget transforms the way Victorians access mental health and wellbeing services, with a greater focus on earlier interventions and outcome-driven support.

### **Box 3.1: The economic case for sustained improvements in mental health and wellbeing**

The Royal Commission into Victoria's Mental Health System estimated the cost to the Victorian economy of poor mental health, including government expenditures, was \$14.2 billion in 2018-19. This includes a cost of \$1.9 billion to employers from productivity loss and workplace injuries. In addition, the monetary cost associated with diminished health and premature death from mental illness is up to two times greater than the cost to the Victorian economy.

The Royal Commission into Victoria's Mental Health System estimated that if the mental health system can be enhanced to achieve a 15 per cent reduction in the level of need, this will deliver \$1.1 billion in additional economic activity in Victoria annually. This includes \$182 million in higher productivity and \$880 million in greater workforce participation among individuals providing unpaid care or not in the labour force.

The Government is introducing a Mental Health and Wellbeing Levy to support a substantial uplift in investment in Victoria's mental health system. This will ensure that investment is sustainable and supports ongoing economic benefits.

Successful system reform that prioritises early intervention requires a strong partnership with the Commonwealth Government. In addition to delivering on its responsibilities in primary care, the Commonwealth must match Victoria's ambition in transforming community-based mental health and wellbeing services. This requires new funding and seamless pathways between services alongside clear role delineation in terms of delivery and funding responsibilities. The Victorian Government will work together with the Commonwealth to develop a new National Agreement on Mental Health and Suicide Prevention to achieve the best outcomes for Victorians.

## **Embedding treatment and support in the community to enable earlier access**

Providing accessible care closer to home and as soon as issues arise can reduce the need for more serious crisis interventions.

Many Victorians experiencing moderate or enduring mental illness cannot be supported through primary care alone, yet their mental illness is not severe enough for specialist mental health services. The Royal Commission into Victoria's Mental Health System estimated that more than two-thirds of demand for community-based mental health services went unmet in 2019-20.

The Government is investing \$264 million to establish 20 new adult and older adult local mental health and wellbeing services. This new model of care will provide a front-door for Victorians to access timely local treatment and support in the community, before they need to access a hospital or reach a crisis point.

A further \$954 million will establish 22 reformed adult and older adult area mental health and wellbeing services to meet more complex needs in the community.

## **Investing in early life services**

Investing in perinatal, children's and young peoples' mental health and wellbeing has the potential to improve the lifetime mental health of future generations.

Mental illness in children and young people can have devastating and life-long consequences, with more than two-thirds of their mental health problems emerging before they are 25 years of age. This is a growing concern, with 34 per cent of surveyed young people from 12 to 25 years of age reporting high or very high psychological distress in 2020, more than three times the rate reported in 2007 (9 per cent).

To address this, the Government is providing \$196 million to establish a dedicated service stream for new parents and children up to 11 years of age within the new integrated system – and \$266 million to ensure Victorians from 12 to 25 years of age receive ongoing dedicated care through Youth Area Mental Health Services, including extended and after-hours support, and support organisations delivering mental health care to young people.

The Government is also investing \$218 million to provide mental health and wellbeing support for students in primary and secondary schools. This funding will establish a Schools Mental Health Fund and expand the Mental Health in Primary Schools pilot to promote evidence-based mental health initiatives in education settings.



## **Setting the foundations to support those most in need**

Alleviating mental illness, particularly for the most vulnerable Victorians, goes beyond the mental health and wellbeing system and requires close collaboration and integration with other government services.

Victorians accessing public specialist mental health services are eight times more likely to access homelessness support. Appropriate and available social housing provides the foundations for effective mental health treatment, so this budget provides \$46 million in supported housing for adults and young people living with mental illness.

Aboriginal Victorians are three times more likely to experience high to very high psychological distress compared with non-Aboriginal Victorians. This budget provides \$116 million to support Aboriginal social and emotional wellbeing as well as funding to support services to provide culturally safe care.

Funding of \$31 million is provided to improve mental health outcomes for people in contact with, or at risk of coming into contact with, the criminal and youth justice systems.

## **Embedding a place-based and outcome driven approach**

This budget supports the Royal Commission's recommendations to restructure governance and implement a new outcomes-focused approach that holds services and government more accountable. Funding of \$34.8 million is provided to establish new regional governance structures that tailor and organise health and wellbeing services to respond directly to local needs.

A further \$71.2 million is provided to strengthen the system through initiatives including a Mental Health and Wellbeing Outcomes Framework and a new Mental Health and Wellbeing Commission. These will enable the collection and monitoring of a new suite of information to improve accountability of outcomes across government portfolios, and support the promotion of good mental health and wellbeing for Victorians.

## **OTHER EARLY INTERVENTION INVESTMENTS AND PARTNERSHIPS ADDRESSING DISADVANTAGE**

Changing the current service landscape and acute service demand trend requires a significant and sustained investment in early intervention. The way forward is to apply an approach to funding early intervention initiatives that can clearly deliver two goals:

- improving outcomes for Victorians by providing timely assistance that effectively addresses their service needs; and
- reducing the usage of acute services that would be required on the current trends.

To realise these benefits, significant expansion of early intervention service capacity is needed at a scale that supports demonstratable impacts.

The Government has invested in programs such as Partnerships Addressing Disadvantage (PADs) that show early intervention can achieve sustained results. For example, the Journey to Social Inclusion (J2SI) PAD is an early intervention program that helps previously homeless Victorians maintain stable housing and minimise their use of emergency hospital services.

Results from the first outcomes measurement of the J2SI PAD showed that 92.9 per cent of program participants were in stable housing. The J2SI cohort have also reduced their hospital bed use by 62 per cent. These results indicate an excellent level of program achievement and, if replicated across the program length, would deliver \$28 million in avoided costs.

This year, the Budget is providing a further \$324 million over four years towards ten initiatives that intervene early and direct effort away from acute services. To support this new approach and help build on it in the future, the Government is also developing an Early Intervention Investment Framework. Similar to the New Zealand wellbeing budget model, this framework will closely track the success of these programs in delivering specific outcomes – and make sure fewer Victorians end up needing acute services.

The package includes initiatives that offer early support to a diverse range of Victorians. This includes people with chronic health conditions or patients waiting to receive elective surgery; Victorians who are at risk of chronic homelessness; families showing early signs of vulnerability and at risk of interacting with the statutory child protection system; and disengaged young people. The Government will build on these investments in future budgets.

**Table 3.1: Select early intervention investments**

<i>Initiative</i>	<i>Portfolio</i>	<i>Department</i>	<i>Funding (\$ million, five year total)</i>
Engaging and supporting at-risk young people	Youth	DFFH	18.4
Early intervention and diversion	Child Protection	DFFH	70.3
Tackling rough sleeping	Housing	DFFH	26.1
Putting Families First	Child Protection	DFFH	17.8
100 000 lives	Health	DoH	45.5
Driving shorter wait lists and better outcomes from elective surgery	Health	DoH	21.6
Legal assistance and critical early intervention support services	Attorney-General	DJCS	31.1
Crime Prevention initiatives	Crime Prevention	DJCS	19.9
Giving vulnerable and disadvantaged kids the best start in life	Early Childhood	DET	33.8
Marrung (Koorie Initiatives Package)	Education/Early Childhood	DET	39.3
<b>Total</b>			<b>324</b>

*Note: Figures in this table are subject to rounding and may not add up to total*

### **Improved outcomes will benefit people now and in the future**

Initiatives in this package will target improving participants' outcomes in a meaningful and measurable way that increases their wellbeing. A broad range of improved outcomes is expected, including:

- a safer and more nurturing environment for children through the provision of family services to parents in more accessible places;
- increased educational achievement and improved school attendance by giving more support to Koorie parents to help grow their skills and confidence in being first educators; and
- reducing the rate of youth justice incidents and other interactions with child protection as high-risk families work with a lead practitioner and team to build resilience and self-manage adversity.

**Box 3.2: Tackling rough sleeping**

The Tackling rough sleeping initiative invests \$26.1 million to intervene early and prevent people at very high risk of homelessness and rough sleeping falling into chronic homelessness by providing stable housing and assistance.

By assisting program participants sustain their housing, gain training and employment, and establish stronger social connections, the initiative will help reduce pressures on other acute services, such as health, housing, police and corrections.

If successful, reductions in service use stemming from the intervention could produce avoided costs representing an estimated return on investment of \$1.84 for every \$1 invested.

**Improved outcomes will reduce avoidable costs**

By focusing on improving outcomes, early intervention initiatives will help avoid Victorians progressing into more acute services, which are generally more intrusive and expensive. The scale of related avoided costs is estimated to be large, including:

- up to \$93 000 per program participant by diverting young people away from criminal activities;
- around \$65 million by targeting preventable hospital admissions, and unnecessary interventions; and
- upwards of \$53 million across health services, human services and justice services by supporting Victorians at risk of falling into chronic homelessness.

**Box 3.3: Putting Families First**

The \$17.8 million Putting Families First initiative aims to improve outcomes for families with multiple complex needs – reducing recidivism and reoffending, improving parenting practices and prosocial behaviours, and increasing school attendance.

At the centre of the initiative is the connection of families to a lead practitioner and support team that will work with the whole family to access therapeutic care. A further team of professionals will be on hand to help with legal, financial and housing matters.

Supporting families to deal with issues early and build their parenting capability will mean that children can remain safely with their family and associated costs to the service system will be reduced over the longer term.

## **Next steps in early intervention**

To support investment in early intervention services, the Government has developed an Early Intervention Investment Framework (EIIIF) that links investment to measurable impacts on both the outcomes of people using the services and the service system.

Funding of \$15.4 million is provided to implement the EIIIF, including further development of methods to measure and track outcomes, avoided costs and impacts of interventions on acute service demand. The methodology will incorporate linked administrative data to ensure initiatives are appropriately targeted and properly measured. This work is expected to help inform future funding decisions.

To continue testing early intervention approaches, this budget provides \$25.8 million over five years for the development of a new PAD to address entrenched disadvantage focused on solutions to address homelessness. Development of the PAD will commence this year with the intervention to target the maximum impact on participant outcomes and avoidable costs.

This builds on the Government's commitment to innovative social investments including four existing partnerships with Anglicare Victoria and VincentCare, Sacred Heart Mission, Melbourne City Mission, and Berry Street and the Victorian Aboriginal Child Care Agency.



## CHAPTER 4 – BUDGET POSITION AND OUTLOOK

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- The *2021-22 Budget* outlines the improvement in the Government’s fiscal position as the Victorian economy recovers from the peak of the coronavirus (COVID-19) pandemic, with a return to an operating cash surplus forecast from 2022-23.
- In this budget, the Government is announcing \$19.0 billion in new output initiatives and \$7.1 billion total estimated investment (TEI) in new asset initiatives.
- The combined impact of an increase in state-based revenues along with new revenue initiatives and efficiency measures has resulted in forecast operating cash surpluses of \$1.1 billion in 2022-23, increasing to \$3.0 billion in 2024-25. This improvement is the result of the Government’s comprehensive and deliberate fiscal strategy that was set out in the *2020-21 Budget*.
- Operating deficits (net result from transactions) are forecast over the budget and forward estimates. However, these estimates reflect a significant improvement relative to the *2020-21 Budget*.
- Total revenue for the general government sector is expected to be \$74.6 billion in 2021-22, an upgrade of \$3.3 billion forecast in the *2020-21 Budget*. Revenue growth is then expected to average 4.6 per cent a year over the forward estimates, reaching \$85.3 billion in 2024-25.
- Total expenditure is expected to reach \$86.2 billion in 2021-22, before reducing by 2.9 per cent in 2022-23, reflecting the targeted and short-term nature of initiatives to fund the public health response and support the economy from the impacts of the pandemic. Expenditure is then forecast to grow by 1.4 per cent in 2023-24 and 2.9 per cent in 2024-25, reaching \$87.4 billion in 2024-25.
- Government infrastructure investment (GII) is expected to average \$22.5 billion a year over the budget and forward estimates, reflecting the continuation of Victoria’s Big Build.
- Net debt is projected to be \$156.3 billion by June 2025, lower in each year of the forward estimates than was forecast in the *2020-21 Budget*, principally due to improvements in the operating position.
- Interest expense as a share of total revenue remains manageable and is expected to average 4.7 per cent a year over the budget and forward estimates.
- The Government is on track to fully fund the State’s unfunded superannuation liability by 2035.

This chapter outlines the budget position of the general government sector. The budget takes into account the financial impacts as at 12 May 2021 of all policy decisions made by the Government, as well as other information that affects the financial statements, unless otherwise stated.

The Budget does not account for the grants and funding agreements announced by the Commonwealth Government as part of the *2021-22 Commonwealth Budget*, which are subject to negotiation and confirmation with the Victorian Government. Many of the infrastructure initiatives and funding agreements are contingent on the Victorian Government sharing the costs. As such, Victoria will consider these initiatives and their suitability with the State's forward infrastructure agenda.

## GENERAL GOVERNMENT SECTOR

### Overview

The *2021-22 Budget* outlines the Government's ongoing commitment to sound financial management as the Victorian economy emerges from the most severe economic effects of the coronavirus (COVID-19) pandemic by acquitting progress against the four-step fiscal strategy for the medium term outlined in the *2020-21 Budget*.

- **Step 1:** creating jobs, reducing unemployment and restoring economic growth;
- **Step 2:** returning to an operating cash surplus;
- **Step 3:** returning to operating surpluses; and
- **Step 4:** stabilising debt levels.

Early signs are that the Government's stimulus strategy is working. The State's economic recovery is well underway and progressing strongly. Employment and workforce participation have already recovered to pre-coronavirus levels. The interim employment target of 200 000 jobs in the Government's *Jobs Plan*, announced as part of the *2020-21 Budget*, has been achieved ahead of schedule.

The net cash flows from operating activities for the general government sector is forecast to be in surplus by \$1.1 billion in 2022-23, increasing to \$3.0 billion in 2024-25, a significant achievement compared with the position in the *2020-21 Budget*.

Returning to an operating surplus (net result from transactions) remains a key priority for the Government. While the Government is still forecasting operating deficits across the forward estimates, these are now significantly smaller than those in last year's budget.



**Table 4.1: General government fiscal aggregates**

	<i>Unit of measure</i>	<i>2019-20 actual</i>	<i>2020-21 revised</i>	<i>2021-22 budget</i>	<i>2022-23 estimate</i>	<i>2023-24 estimate</i>	<i>2024-25 estimate</i>
Net result from transactions	\$ billion	(6.5)	(17.4)	(11.6)	(3.8)	(2.1)	(2.1)
Net cash flows from operating activities	\$ billion	(2.9)	(17.4)	(2.0)	1.1	2.4	3.0
Government infrastructure investment <sup>(a)(b)</sup>	\$ billion	12.0	14.5	24.2	21.7	22.7	21.6
Net debt	\$ billion	44.3	77.5	102.1	120.0	138.3	156.3
Net debt to GSP <sup>(c)</sup>	per cent	9.5	16.7	20.3	22.7	24.9	26.8

Source: Department of Treasury and Finance

Notes:

- (a) Includes general government net infrastructure investment and estimated construction costs of public private partnership projects.
- (b) Includes the estimated private sector construction related expenditure associated with the North East Link held in the public non-financial corporations (PNFC) sector.
- (c) The ratios to gross state product (GSP) may vary from publications year to year due to revisions to the Australian Bureau of Statistics GSP data.

Government infrastructure investment (GII) is expected to average \$22.5 billion a year over the budget and forward estimates, reflecting the continuation of Victoria’s Big Build.

In the *2020-21 Budget*, net debt was forecast at \$154.8 billion by June 2024. Now this level is not forecast until June 2025, with net debt by this time projected to be \$156.3 billion.

Total revenue for the general government sector is expected to be \$74.6 billion in 2021-22, an upgrade of \$3.3 billion compared with the *2020-21 Budget* largely due to the stronger than expected economic recovery from COVID-19. Revenue is expected to grow by an average of 4.6 per cent a year over the forward estimates to \$85.3 billion in 2024-25.

The increase in revenue is a combination of a stronger economy and the Government strengthening its revenue base through the introduction of targeted new revenue initiatives.

This budget invests \$19.0 billion in new output initiatives and \$7.1 billion TEI in new asset initiatives.

Expenditure in 2021-22 is expected to be \$86.2 billion which includes short-term, targeted initiatives to support Victorians and drive the economic recovery, with average growth across the forward estimates expected to be a moderate 0.5 per cent a year, increasing to \$87.4 billion by 2024-25.

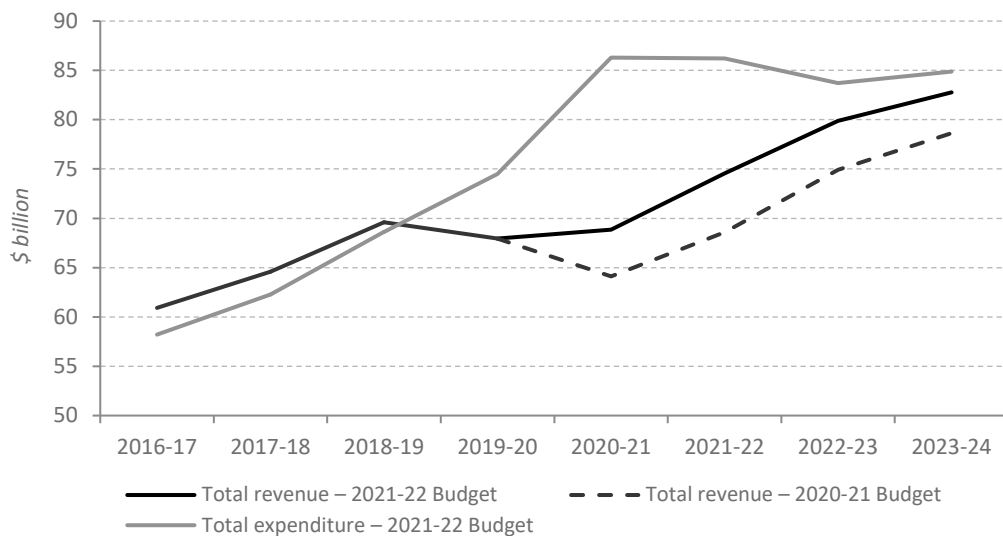
To achieve progress in moving to a more balanced operating position, expenditure will be redirected to ensure the continued efficient and effective delivery of government priorities. Expenditure will also be reviewed on an ongoing basis to ensure lower value spending is reprioritised and invested in priority areas.

In recognition of a low inflation environment, indexation applied to departments’ base funding will be revised with differentiated rates provided for wage and non-wage components. Non-wage indexation will be guided by the Government’s consumer price index forecasts. Wage indexation will be aligned to the Government’s rebalanced wages policy, with impacts to be phased in from 1 January 2022.

This initiative is part of the Government’s comprehensive strategy to return to an operating surplus in the medium term.

A key challenge of fiscal sustainability is realigning revenue and expenditure. The 2021-22 Budget demonstrates improved performance against this objective. The strong economic recovery, coupled with a strengthening of the revenue base, drives significant upgrades to revenue forecasts that narrows the gap between revenue and expenditure forecasts in the 2020-21 Budget.

**Chart 4.1: Revenue from transactions between 2021-22 Budget and 2020-21 Budget <sup>(a)</sup>**



Source: Department of Treasury and Finance

Note:

(a) To improve comparability in this chart, revenue and expenditure in both the 2020-21 Budget and 2021-22 Budget excludes the impacts of the Capital Assets Charge (CAC) policy levied on VicTrack following the discontinuation of the policy from 2021-22.

## BUDGET AND FORWARD ESTIMATES OUTLOOK

Table 4.2 summarises the operating statement for the general government sector. A comprehensive operating statement is presented in Budget Paper No. 5, Chapter 1 *Estimated Financial Statements for the general government sector*.

**Table 4.2: Summary operating statement for the general government sector <sup>(a)</sup> (\$ million)**

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25
	actual	revised	budget	estimate	estimate	estimate
<b>Revenue and income from transactions</b>						
Taxation	23 167	23 468	26 577	29 058	31 097	32 429
Dividends, TER and interest <sup>(b)</sup>	1 429	1 226	1 212	1 175	1 235	1 246
Sales of goods and services <sup>(c)</sup>	7 902	8 059	6 405	6 526	6 645	6 716
Grants	32 789	35 743	36 778	39 695	40 527	41 520
Other revenue and income	2 662	2 923	3 605	3 414	3 268	3 383
<b>Total revenue and income from transactions</b>	<b>67 948</b>	<b>71 419</b>	<b>74 576</b>	<b>79 868</b>	<b>82 773</b>	<b>85 295</b>
% change	(2.4)	5.1	4.4	7.1	3.6	3.0
<b>Expenses from transactions</b>						
Employee expenses	27 214	29 205	31 725	32 590	33 542	34 255
Superannuation <sup>(d)</sup>	3 480	3 628	4 247	4 285	4 361	4 434
Depreciation	3 894	4 216	4 399	4 572	4 770	5 273
Interest expense	2 328	2 832	3 051	3 499	4 069	4 774
Grant expense <sup>(c)</sup>	15 331	21 691	17 301	15 133	14 777	14 995
Other operating expenses	22 241	27 290	25 477	23 625	23 359	23 650
<b>Total expenses from transactions</b>	<b>74 487</b>	<b>88 862</b>	<b>86 200</b>	<b>83 705</b>	<b>84 879</b>	<b>87 379</b>
% change	8.5	19.3	(3.0)	(2.9)	1.4	2.9
<b>Net result from transactions – net operating balance</b>	<b>(6 539)</b>	<b>(17 443)</b>	<b>(11 624)</b>	<b>(3 837)</b>	<b>(2 106)</b>	<b>(2 085)</b>
<b>Total other economic flows included in net result <sup>(e)</sup></b>	<b>(1 360)</b>	<b>(755)</b>	<b>(471)</b>	<b>(446)</b>	<b>(440)</b>	<b>(398)</b>
<b>Net result</b>	<b>(7 899)</b>	<b>(18 198)</b>	<b>(12 094)</b>	<b>(4 283)</b>	<b>(2 547)</b>	<b>(2 483)</b>

Source: Department of Treasury and Finance

Notes:

- (a) Figures in this table are subject to rounding to the nearest million and may not add up to totals.
- (b) Comprises dividends, income tax and rate equivalent revenue and interest.
- (c) As highlighted in Budget Paper No. 3, Chapter 2 Departmental Performance Statements, the CAC policy is discontinued from 2021-22. The removal of CAC reduces the Sales of goods and services and Grant expense by the same amount.
- (d) Comprises superannuation interest expense and other superannuation expenses.
- (e) This typically includes gains and losses from the disposal of non-financial assets, adjustments for bad and doubtful debts and revaluations of financial assets and liabilities.

## Revenue outlook

Total revenue for the general government sector is expected to increase by 4.4 per cent to \$74.6 billion in 2021-22, with growth projected to average 4.6 per cent a year over the forward estimates. Revenue recognised in 2019-20 and 2020-21 was materially suppressed due to the impact of the pandemic and support initiatives provided by the Government.

Compared with the *2020-21 Budget*, taxation revenue, goods and services tax (GST) grants and most other revenue streams have been upgraded, reflecting the strong economic recovery and the introduction of targeted revenue initiatives. Since the *2020-21 Budget*, total revenue has increased by \$3.3 billion in 2021-22, \$2.1 billion in 2022-23 and by \$1.3 billion in 2023-24, reflecting significant recovery of the write-downs in revenues included in the previous budget. This is partially offset by the discontinuation of the Capital Assets Charge (CAC) policy levied on VicTrack from 2021-22. The removal of CAC reduces the revenue from sales of goods and services and grant expenses by the same amount.

## Taxation

State taxation revenue is forecast to increase by 13.2 per cent in 2021-22, as it recovers from suppressed levels in 2019-20 and 2020-21 due to the impact of the pandemic and support initiatives provided by the Government to support households, workers and businesses. Taxation revenue is expected to grow by an average annual rate of 6.9 per cent a year over the forward estimates, reflecting an improved outlook for most taxes and new policy initiatives.

- Land transfer duty is expected to increase by 12.7 per cent to \$6.7 billion in 2021-22 after a fall of 3.1 per cent in 2020-21, driven by the strong recovery in property transaction prices and volumes flowing through to revenue and the introduction of a premium rate on land transfer duty for high-value properties. Strong growth is expected to continue in 2022-23 before slowing down from 2023-24 onwards as the cycle matures with weak wage and population growth putting downward pressure on property prices and volumes. Land transfer duty is expected to grow by an average of 6.2 per cent a year over the forward estimates.
- Land tax revenue is expected to increase by 15.2 per cent to \$4.2 billion in 2021-22, as a result of an improved outlook for residential and commercial land values relative to the *2020-21 Budget*, the end of land tax relief under the Support to Landlords and Tenants package, and an increase in land tax rates for the two highest thresholds. Land tax revenue is expected to grow by an average of 9.0 per cent a year over the forward estimates.
- Payroll tax revenue is forecast to decline by 0.9 per cent to \$6.1 billion in 2021-22, reflecting the impact of payroll tax relief initiatives to eligible businesses, partially offset by a strong labour market recovery. Payroll tax revenue is expected to grow by an average of 8.3 per cent a year over the forward estimates as the labour market continues to recover.

- Gambling tax revenue is forecast to recover in 2021-22, increasing by 50.2 per cent to \$2.3 billion. This reflects the reopening of gaming venues, after their temporary closure in the 2020 calendar year as part of the public health response to the pandemic, which materially suppressed the revenue levels in both 2019-20 and 2020-21. Gambling tax revenue is forecast to grow by an average of 2.9 per cent a year over the forward estimates.
- Motor vehicle taxes are expected to increase by 7.0 per cent to \$2.9 billion in 2021-22 after a modest increase of 1.9 per cent in 2020-21. Motor vehicle taxes are expected to grow by an average of 4.8 per cent a year over the forward estimates. Improved consumer confidence is expected to support growth in motor vehicle taxes over the budget and forward estimates.
- Insurance taxes are expected to increase by 7.2 per cent in 2021-22 to \$1.6 billion after a 2.2 per cent increase in 2020-21. Insurance taxes are expected to grow by an average of 6.4 per cent a year over the forward estimates.
- Revenue from the new Mental Health and Wellbeing Levy, which commences on 1 January 2022 is estimated to raise \$387 million in 2021-22, and an average of \$843 million each year over the forward estimates. The Government will legislate that revenue from this levy will only fund mental health services, supporting a substantial increase in investment in Victoria's mental health system.

Details of specific new revenue policy initiatives are contained in Budget Paper No. 3, Chapter 1 *Output, Asset Investment, Savings and Revenue Initiatives*.

### **Dividends, income tax equivalent and interest**

Dividend and income tax equivalent revenue is projected to decline by 3.3 per cent in 2021-22, before increasing by an average of 0.5 per cent a year over the forward estimates. The lower revenue in 2021-22 is primarily due to lower profits of the metropolitan water corporations, reflecting the impact of the pandemic on business customers and provision of hardship relief for customers impacted during the pandemic.

Interest revenue is received on the cash and deposits held by government. Total interest is expected to be \$0.6 billion in 2021-22, and is forecast to increase by an average of 1.3 per cent a year over the forward estimates.

### **Sales of goods and services**

Revenue generated by the sales of goods and services is forecast to decline by 20.5 per cent in 2021-22 to \$6.4 billion, driven by the discontinuation of the CAC policy levied on VicTrack from 2021-22. The removal of CAC reduces the revenue from the sales of goods and services and grant expenses by the same amount.

Excluding movements associated with the discontinuation of CAC, sales of goods and services is forecast to increase by 16.6 per cent in 2021-22. This largely reflects the expected recovery in various government service fees after the easing of public health restrictions. Growth is expected to average 1.6 per cent a year over the forward estimates.

## Grants

Total grant revenue is expected to increase by 2.9 per cent in 2021-22 to \$36.8 billion. Grants recognised by the State are largely in respect to GST and grants for specific purposes.

Victoria's GST revenue is expected to grow by 2.0 per cent in 2021-22. More robust labour market conditions, higher asset prices and improved consumer confidence have contributed to a sharper recovery in national household consumption and dwelling investment, leading to a stronger outlook for the national GST pool. The improvement in the outlook for the national GST pool in 2021-22 is partially offset by a weaker assessed Victorian relativity and a lower than expected share of the national population, following the closure of national borders.

Over the forward estimates, GST revenue is expected to grow by an average rate of 4.8 per cent a year, primarily driven by growth in the national GST pool, which is expected to moderate, reflecting the impact of slower growth in the national population. Victoria's assessed relativity is forecast to decrease over the forward estimates. Under the revised GST methodology, Victoria will continue to receive less than its fair share of GST revenue relative to its population.

Commonwealth grants for specific purposes are projected to average \$19.8 billion a year over the next four years. The Commonwealth provides these grants as contributions toward healthcare, education, disability, major infrastructure investment and other services.

## Other revenue and income

Other revenue and income includes fines, royalties, donations and gifts, assets received free-of-charge and other miscellaneous revenues. Other revenue is expected to grow by 23.3 per cent to \$3.6 billion in 2021-22, followed by an average decline of 2.1 per cent a year over the forward estimates. This revenue profile is largely driven by the receipt of infrastructure assets free-of-charge from the Metro Tunnel settlement, which peak in 2021-22.

Budget Paper No. 5, Chapter 4 *State Revenue* contains further details of expected movements in the major categories of general government revenue.

## Expenses outlook

The Government is expected to spend \$86.2 billion in 2021-22. While this is slightly lower than the forecast total expenditure of \$88.9 billion in 2020-21, this level is higher than pre-coronavirus levels as the Government continues to support Victorians and economic recovery during the pandemic. Expenses are then expected to decline by 2.9 per cent in 2022-23 reflecting the tapering of direct economic support before increasing by 1.4 per cent and 2.9 per cent in 2023-24 and 2024-25 respectively to \$87.4 billion in 2024-25. Moderation of expenditure growth over the forward estimates is driven in part by efficiencies and savings measures.

As outlined in Budget Paper No. 3, Chapter 2 *Department Performance Statements*, the CAC policy will be discontinued from the 2021-22 Budget, consistent with the approach taken by other states. This will not impact on departments' service delivery as departments were funded from the budget for their CAC expense, and then immediately paid the same amount back into the Consolidated Fund.

However, the discontinuation of this policy reduces the total revenue and expenditure figures for the general government sector as the CAC applied to VicTrack, which sits outside the general government sector. Funding for the CAC was provided to VicTrack from the general government sector (as an expense) which was then returned to the general government sector (as revenue), resulting in a budget neutral outcome.

Table 4.3 shows the profile of total expenditure for the general government sector for the 2021-22 Budget and 2020-21 Budget on a like-for-like basis, that is, excluding the CAC-related expenditure to VicTrack.

**Table 4.3: Comparison of total expenditure between the 2021-22 Budget and 2020-21 Budget (excluding CAC)** (\$ million)

	2021-22 budget	2022-23 estimate	2023-24 estimate	2024-25 estimate <sup>(c)</sup>
2021-22 Budget – Total expenses <sup>(a)</sup>	86 200	83 705	84 879	87 379
2020-21 Budget – Total expenses <sup>(a)(b)</sup>	81 676	81 656	84 522	n.a.
<b>Increase in total expenditure</b>	<b>4 524</b>	<b>2 049</b>	<b>358</b>	<b>n.a.</b>

Source: Department of Treasury and Finance

Notes:

(a) Excludes the impacts of the CAC policy levied on VicTrack following the discontinuation of the policy from 2021-22.

(b) Published figures for total expenditure in the 2020-21 Budget were \$84.4 billion in 2021-22, \$84.5 billion in 2022-23 and \$87.3 billion in 2023-24.

(c) 2024-25 aggregates were not published in the 2020-21 Budget.

This shows that the Government is investing an additional net \$6.9 billion from 2021-22 to 2023-24 compared with the 2020-21 Budget.

The expenditure profile over the budget and forward estimates reflects the targeted support and response provided by the Government to the pandemic.

- Employee expenses (including superannuation) are forecast to grow by 9.6 per cent in 2021-22. The growth over the budget and forward estimates reflects the Government's response to the pandemic, increased service delivery, primarily in public health, mental health and education and an increase in the superannuation interest expense on the State's defined benefit superannuation liability attributable to an increase in bond yields. It also includes the impact of re-balancing the Government's wages policy. Average growth over the forward estimates of 2.5 per cent a year is forecast, consistent with the requirements of service delivery and enterprise bargaining agreements.
- Depreciation expense is forecast to grow by an average of 5.7 per cent over the budget and forward estimates from \$4.2 billion in 2020-21 to \$5.3 billion by 2024-25. Growth in depreciation is broadly in line with continuing Victoria's high levels of investment in transport infrastructure.

- Interest expense is forecast to grow by 7.7 per cent to \$3.1 billion in 2021-22, and by an average of 16.1 per cent a year over the forward estimates, as the Government increases borrowings to fund its response to the pandemic and continue significant levels of infrastructure investment under Victoria’s Big Build. Interest expense as a share of total revenue is expected to remain manageable, averaging 4.7 per cent a year over the budget and forward estimates, well below the historical levels seen during the 1990s.
- Grants expenses are forecast to reduce by 20.2 per cent in 2021-22 reflecting the discontinuation of the CAC policy levied on VicTrack from 2021-22 and the tapering of support to businesses and individuals provided by the Government’s economic support during the pandemic. A further 12.5 per cent reduction in grant expenditure in 2022-23 reflects the further tapering of pandemic support. Grants expenses are then expected to moderate, reducing by 2.4 per cent in 2023-24 and growing by 1.5 per cent in 2024-25.
- Other operating expenses are forecast to decline by 6.6 per cent in 2021-22 and by an average of 2.5 per cent a year across the forward estimates as expenditure attributable to the Government’s COVID-19 response tapers.

**Box 4.1: Drawdown of Treasurer’s Advance appropriation**

The *Appropriation (Interim) Act 2020* (the Supply Act) provided a Treasurer’s Advance (TA) appropriation of \$14.5 billion for the first half of the 2020-21 financial year.

This ensured that the Government had sufficient access to funding to supplement other funding sources such as grants from the Commonwealth and special appropriations to respond to the pandemic.

\$3.4 billion was drawn down under the TA in the Supply Act for 2020-21 prior to the *Appropriation (2020-21) Act 2020* subsuming the Supply Act, upon receiving Royal Assent on 15 December 2020. Amounts of supplementary funding provided to departments from the 2020-21 TA appropriated by the Supply Act were incorporated within those departments’ annual appropriations in the *Appropriation (2020-21) Act 2020*.

The *Appropriation (2020-21) Act 2020* provides the appropriation amounts for 2020-21 agreed by Parliament.



## Reconciliation of estimates to the 2020-21 Budget

Relative to the 2020-21 Budget, the net result from transactions has been revised up by \$1.5 billion in 2021-22, \$2.9 billion in 2022-23 and by \$3.8 billion in 2023-24 (Table 4.4).

**Table 4.4: Reconciliation of estimates to the 2020-21 Budget** <sup>(a)</sup> (\$ million)

	2021-22 budget	2022-23 estimate	2023-24 estimate
<b>Net result from transactions: 2020-21 Budget</b>	<b>(13 098)</b>	<b>(6 725)</b>	<b>(5 889)</b>
<b>Policy variations</b>			
Revenue policy initiatives <sup>(b)</sup>	855	1 476	1 576
Output policy initiatives <sup>(c)</sup>	(5 739)	(3 509)	(2 043)
	<b>(4 884)</b>	<b>(2 033)</b>	<b>(467)</b>
<b>Economic/demographic variations</b>			
Taxation	1 894	1 397	1 717
Investment income <sup>(d)</sup>	81	8	(32)
	<b>1 975</b>	<b>1 405</b>	<b>1 685</b>
<b>Commonwealth grant variations</b>			
General purpose grants	1 468	928	(140)
Specific purpose grants <sup>(e)</sup>	185	436	246
	<b>1 654</b>	<b>1 364</b>	<b>105</b>
<b>Administrative variations</b>			
Contingency offset for new policy initiatives <sup>(f)</sup>	250	300	350
Other administrative variations	2 479	1 853	2 109
	<b>2 729</b>	<b>2 153</b>	<b>2 459</b>
<b>Total variation since 2020-21 Budget</b>	<b>1 474</b>	<b>2 888</b>	<b>3 782</b>
<b>Net result from transactions: 2021-22 Budget</b>	<b>(11 624)</b>	<b>(3 837)</b>	<b>(2 106)</b>

Source: Department of Treasury and Finance

Notes:

- (a) Figures in this table are subject to rounding to the nearest million and may not add up to totals.
- (b) Includes revenue from the Mental Health and Wellbeing Levy, which is offset by expenditure implementing the recommendations of the Royal Commission into Victoria's Mental Health System.
- (c) This is represented in Table 4.5 as the 2021-22 Budget output policy initiatives.
- (d) Comprises dividends and income tax and rate equivalent revenue.
- (e) Reflects the change in grant revenue as per Note 1.2.4 of Budget Paper No. 5, Chapter 1 Estimated Financial Statements for the general government sector less associated expense movements.
- (f) Represents releases from the funding not allocated to specific purposes contingency associated with 2021-22 Budget new output initiatives. Further information on total output contingencies can be found at Note 1.3.5 of Budget Paper No. 5, Chapter 1 Estimated Financial Statements for the General Government Sector.

### Policy variations

Policy variations reflect specific initiatives by the Government that have a fiscal impact over the next four years and are related to a new policy or represent a change in the Government's existing policy position since the 2020-21 Budget.

New revenue policy initiatives included in the 2021-22 Budget raise \$5.6 billion over four years.

The 2021-22 Budget funds \$19.0 billion in new output initiatives over the five years to 2024-25. Table 4.5 shows the impact of the new output initiatives in this budget.

Details of specific new output and revenue policy initiatives are contained in Budget Paper No. 3, Chapter 1 *Output, Asset Investment, Savings and Revenue Initiatives*.

**Table 4.5: Net impact of the 2021-22 Budget new output initiatives <sup>(a)</sup> (\$ million)**

	2021-22 budget	2022-23 estimate	2023-24 estimate	2024-25 estimate
<b>New output initiatives</b>	<b>6 579</b>	<b>4 133</b>	<b>3 511</b>	<b>3 463</b>
Less:				
Reprioritisations and revenue offsets <sup>(b)</sup>	939	611	622	704
Adjustments <sup>(c)</sup>	(198)	(156)	155	337
Savings	99	168	690	925
<b>2021-22 Budget output policy initiatives</b>	<b>5 739</b>	<b>3 509</b>	<b>2 043</b>	<b>1 497</b>
Less: contingency offset for new policy <sup>(d)</sup>	250	300	350	450
<b>Net impact</b>	<b>5 489</b>	<b>3 209</b>	<b>1 693</b>	<b>1 047</b>

Source: Department of Treasury and Finance

Notes:

- (a) Figures in this table are subject to rounding to the nearest million and may not add up to totals.  
(b) This includes the reprioritisation of resources previously allocated to departments and revenue offsets.  
(c) Primarily incorporates the net impact of the specific creation and release of contingencies held for decisions made but not yet allocated.  
(d) Represents releases from the funding not allocated to specific purposes contingency associated with 2021-22 Budget new output initiatives. Further information on total output contingencies can be found at Note 1.3.5 of Budget Paper No. 5, Chapter 1 Estimated Financial Statements for the General Government Sector.

### *Economic and demographic variations*

Since the 2020-21 Budget, taxation revenue has been revised upwards by \$1.9 billion in 2021-22, \$1.4 billion in 2022-23 and by \$1.7 billion in 2023-24 due to economic and demographic variations. This includes upgrades to land transfer duty, payroll tax and land tax revenue estimates, as a result of the strong economic recovery.

### *Commonwealth grants variations*

Commonwealth general purpose grants (or GST grants) have been revised up by \$1.5 billion in 2021-22, \$928 million in 2022-23 and down by \$140 million in 2023-24 compared with the 2020-21 Budget. This reflects a stronger outlook for national consumption and dwelling investment, partly offset by a weaker assessed Victorian relativity and a lower than expected share of the national population.

Net changes to specific purpose grants have increased the operating result by an average of \$289 million a year from 2021-22 to 2023-24 compared with the 2020-21 Budget. The movements primarily reflect additional infrastructure grants.

### *Administrative variations*

Other administrative variations are expected to increase the operating result by \$2.5 billion in 2021-22, \$1.9 billion in 2022-23 and \$2.1 billion in 2023-24. The variations since the 2020-21 Budget include:

- adjustments to the provisions for decisions made but not yet allocated that are outlined in Note 1.3.5 of Budget Paper No. 5, Chapter 1 *Estimated Financial Statements for the General Government Sector*; partially offset by;

- an increase in the superannuation interest expense on the State’s defined benefit superannuation liability due to increases in the bond yields that underlie the key superannuation valuation assumptions; and
- an increase in interest expense in line with increased global bond rates since the 2020-21 Budget.

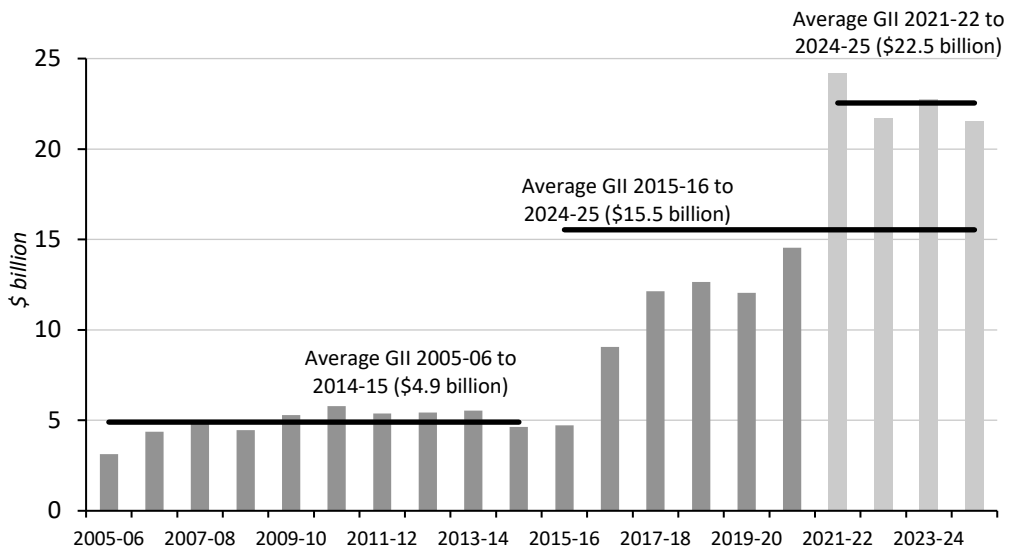
## Capital expenditure

Government infrastructure investment, which measures investment funded by Government and estimated private sector construction related expenditure on public private partnership projects, is expected to average \$22.5 billion a year over the budget and forward estimates. This includes new expenditure in rolling stock, mental health facilities and schools and funding already committed on major productivity-enhancing projects including the North East Link, Metro Tunnel, West Gate Tunnel, Melbourne Airport Rail and the removal of 75 level crossings by 2025.

Further information on the Government’s infrastructure investment, and how it will support jobs and the economic recovery, is available in Budget Paper No. 4, *State Capital Program*.

Budget Paper No. 3, Chapter 1 *Output, Asset Investment, Savings and Revenue Initiatives* contains details of individual asset initiatives.

**Chart 4.2: Government infrastructure investment** <sup>(a)(b)(c)(d)</sup>



Source: Department of Treasury and Finance

Notes:

- Includes general government net infrastructure investment and estimated cash flows for public private partnership projects.
- Includes the estimated private sector construction related expenditure associated with the North East Link held in the PNFC sector.
- Excludes the impact of the medium-term lease over the operations of the Port of Melbourne and the divestment of Victoria’s share of Snowy Hydro Limited.
- The figure for 2020-21 is an estimate.

## Net debt

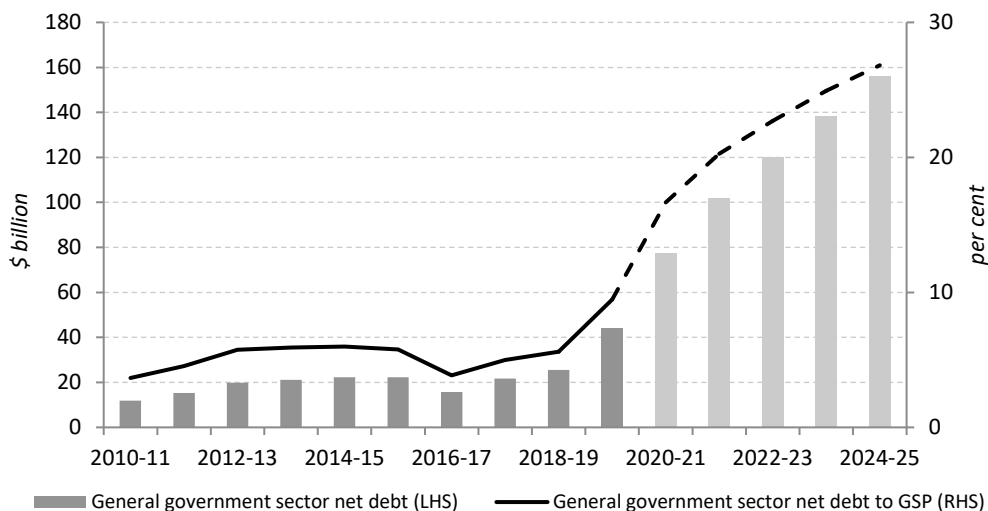
Net debt is projected to be \$102.1 billion at June 2022 and is forecast to increase to \$156.3 billion by June 2025. As a proportion of gross state product (GSP), net debt is projected to increase to 26.8 per cent by June 2025. Net debt is lower in each year than forecast in the *2020-21 Budget*, principally due to the improved operating position.

The *2020-21 Budget* outlined that substantial Government funding of essential services and economic support is required to respond to the pandemic and included a four-step fiscal plan for the medium term, with the final step being the stabilising of debt levels.

Expenditure in response to the pandemic is focussed on the short to medium term to allow required services and economic support to be provided while not compromising progress against the fiscal plan. Coupled with upgrades in the revenue outlook associated with strengthening economic indicators, the net debt outlook has significantly improved since the *2020-21 Budget*. Net debt has been revised down from the *2020-21 Budget* by \$7.6 billion by June 2022, \$12.8 billion by June 2023 and by \$16.4 billion by June 2024.

Further, the achievement of an operating cash surplus from 2022-23 is an important step in stabilising debt as it indicates that from this point the Government’s operating cash payments are fully funded by operating receipts.

**Chart 4.3: General government net debt to GSP**



Source: Department of Treasury and Finance

The application of cash resources for the general government sector (as shown in Table 4.6) outlines the annual movements in net debt.

**Table 4.6: Application of cash resources for the general government sector <sup>(a)</sup> (\$ million)**

	2019-20 actual <sup>(b)</sup>	2020-21 revised	2021-22 budget	2022-23 estimate	2023-24 estimate	2024-25 estimate
<b>Net result from transactions</b>	<b>(6 539)</b>	<b>(17 443)</b>	<b>(11 624)</b>	<b>(3 837)</b>	<b>(2 106)</b>	<b>(2 085)</b>
Add back: Operating cash flows not recognised in the net operating balance <sup>(c)</sup>	3 626	53	9 575	4 904	4 469	5 101
<b>Net cash flows from operating activities</b>	<b>(2 913)</b>	<b>(17 390)</b>	<b>(2 049)</b>	<b>1 067</b>	<b>2 363</b>	<b>3 017</b>
<b>Less: Total net investment in fixed assets <sup>(d)</sup></b>	<b>8 207</b>	<b>11 925</b>	<b>18 692</b>	<b>17 790</b>	<b>19 804</b>	<b>20 825</b>
<b>Surplus/(deficit) of cash from operations after funding net investment in fixed assets</b>	<b>(11 120)</b>	<b>(29 315)</b>	<b>(20 741)</b>	<b>(16 723)</b>	<b>(17 441)</b>	<b>(17 808)</b>
Less:						
Leases and service concession arrangements <sup>(e)</sup>	2 224	3 379	2 087	1 675	1 434	405
Other movements	1 910	528	1 710	(436)	(559)	(231)
<b>Decrease/(increase) in net debt</b>	<b>(15 254)</b>	<b>(33 222)</b>	<b>(24 538)</b>	<b>(17 963)</b>	<b>(18 316)</b>	<b>(17 982)</b>

Source: Department of Treasury and Finance

Notes:

- (a) Figures in this table are subject to rounding to the nearest million and may not add up to totals.
- (b) Movements in 2019-20 include the impact of the new accounting standards.
- (c) Includes depreciation, prepayments and movements in the superannuation liability and liability of employee benefits for the year, and the progressive unwinding of the grant of a right to the operator liability.
- (d) Includes total purchases of plant, property and equipment, and net capital contributions to other sectors of government net of proceeds from asset sales.
- (e) Includes most operating leases which are now required to be recognised as lease liabilities. It also includes the financial liabilities relating to public private partnerships including the High Capacity Metro Trains Project, the Metro Tunnel, the new Footscray Hospital, Frankston Hospital Redevelopment and Western Roads Upgrade.

## Unfunded superannuation liability

The Government is on track to fully fund the State's unfunded superannuation liability by 2035. Note 1.6.3 of Budget Paper No. 5, Chapter 1 *Estimated Financial Statements for the General Government Sector* shows information on the reported superannuation liability.

## **FISCAL RISKS**

This section discusses a number of risks which, if realised, are likely to impact on the State's financial position and budget outcomes.

Details of specific contingent assets and liabilities, defined as possible assets or liabilities that arise from past events, whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity, are contained within Budget Paper No. 5, Chapter 6 *Contingent Assets and Contingent Liabilities*.

### **General fiscal risks**

#### **Coronavirus (COVID-19)**

Further COVID-19 outbreaks domestically, requiring the reintroduction of broad public health restrictions for extended periods present a key downside risk, with this risk more material until the population is widely vaccinated. This would likely lead to renewed falls in consumer spending and employment.

The Government's forecast revenues, expenses and borrowings are predicated on a series of assumptions, including those related to the global recovery. If these assumptions do not eventuate, the actual financial outcomes may differ materially from the Government's current budget.

Appendix A *Sensitivity analysis* contains information on the impact of variations in the macroeconomic outlook on the Government's key fiscal aggregates. This includes a scenario of a protracted global recovery resulting from delays to the effective global roll-out of vaccines leading to renewed outbreaks and restrictions in major economies.

#### ***National Partnership on COVID-19 Response***

To support the national and coordinated health response to the pandemic, in April 2020 the Commonwealth and states agreed shared funding arrangements via a new National Partnership Agreement. The Agreement will operate for the duration of the Australian Health Sector Emergency Response Plan for Novel Coronavirus 2019, declared by the Australian Health Protection Principal Committee with additional time for payment reconciliation. The Agreement does not have a clear sunset date for budget purposes. If the Agreement is terminated prior to 2022-23 before planned pandemic responses cease, this may reduce Commonwealth payments to the State.

## State taxes

State tax forecasts are primarily modelled on the relationships between taxation revenue and projected economic variables. As a result, the main source of uncertainty to state taxation estimates is unforeseen changes in the economic outlook.

Revenue from property-based taxes, such as land tax and land transfer duty, is subject to unique risks and historically have been volatile. The *2021-22 Budget* incorporates the strong recovery in property-related revenue over the budget and forward estimates as well as the introduction of new property-based revenue initiatives. Property markets can exhibit large cycles typically related to changes in interest rates and/or changes in sentiment. If property prices and transaction volumes were to pick up more than anticipated, in the context of a low mortgage interest rate environment, revenue from property-based taxes may be stronger than forecast. On the downside, a protracted global recovery leading to a deterioration in Victoria's economic conditions and slower population growth could lead to weaker collections from property-based taxes. This risk is explored further in Appendix A *Sensitivity analysis*.

## Employee expenses

Employee expenses are the State's largest expense. Two important determinants of employee expenses are wages growth and the number of employees.

Wages growth is primarily driven by enterprise bargaining agreements, which are subject to compliance with the Government's wages policy, which has been re-balanced as part of the savings and efficiency initiatives. Other factors contributing to projected employee expenses include the composition and profile of the workforce as well as rostering arrangements.

## Demand growth

Another key uncertainty is growth in demand for government services exceeding or being below current projections. This can occur, for example, as a result of higher than forecast population growth or expenditure in response to unforeseen events such as natural disasters, including bushfires and floods.

The estimates incorporate contingency provisions to mitigate the impact of expenditure risks, which may be realised during the next four years. The contingency provisions are sized to allow for the likely growth in Victoria's population and the derived increased demand for government services.

Note 1.3.5 and Note 1.3.6 of Budget Paper No. 5, Chapter 1 *Estimated Financial Statements for the General Government Sector* discloses general government output and asset contingencies not allocated to departments.

## Capital program risks

The Government is delivering a historically large program of capital investments aimed at supporting jobs for economic recovery and improving productivity and the quality of public service delivery. In addition to the existing projects in construction, there is a substantial amount of new investment in this budget that will be delivered in the short to medium term.

This elevated level of infrastructure investment in Victoria coincides with similar increases in other Australian jurisdictions. Investment is anticipated to remain elevated over the medium term and constrain some parts of the construction industry and supply chains placing pressure on delivery timetables and costs. To mitigate the impact of these constraints, the Government has implemented a range of strategies to support growth in the construction industry, including freeing up supply chains, an extractive resources strategy and increasing investment in skills.

COVID-19 created some uncertainty on the State's capital program during 2020. The Government has implemented a whole of government framework to assist delivery agencies to manage risks associated with COVID-19 for projects at each stage of the project lifecycle. The framework facilitates outcomes that are best for individual projects, project workforces and broader economic recovery in Victoria. This coordinated approach from the Government is expected to reduce project and financial risk, preserve the project pipeline and sustain competitive local industries.

## Specific fiscal risks

### Commonwealth schools funding

In June 2017, the Commonwealth Government passed amendments to the *Australian Education Act 2013* to implement a new national school funding model. Victoria has signed the National School Reform Agreement and an accompanying bilateral agreement, which expire on 31 December 2023. Estimates of funding required to acquit the Schooling Resource Standard target in a given year will be based on student number and profile projections for that year. Expenditure targets will be finalised towards the end of or after the school year in question based on actual student data, creating a risk that the Victorian and Commonwealth targets differ from the funding allocated that year.

### Universal Access to Early Childhood Education

The Commonwealth's financial contribution to assist the states and territories in providing access to 15 hours a week of kindergarten, in the year before school, is supplied under the National Partnership Agreement on Universal Access to Early Childhood Education. Funding under this agreement expires on 31 December 2021 and ongoing Commonwealth funding arrangements are still to be negotiated. An independent review, led by the Nous Group, found that the agreement achieved its stated objectives and made a range of recommendations including that governments move towards a longer-term agreement to support universal access to high quality early education in the year before school.



## **National Health Reform Agreement Funding Cap**

Under the 2020-25 Addendum to the National Health Reform Agreement, the Commonwealth co-funds public hospitals by contributing 45 per cent of the cost of eligible activity, with the Commonwealth contribution capped at a growth rate of 6.5 per cent compared to the previous year's contribution. This is a "soft cap" that applies at a national level, with states entitled to receive a Commonwealth contribution beyond the cap until the annual growth rate of national expenditure reaches 6.5 per cent. Uncertainty around expenditure growth in other states and territories may create a fiscal risk to the State if the Commonwealth does not fund 45 per cent of additional eligible hospital spending.

## **Victoria's GST revenue**

Victoria's GST revenue is broadly determined by three key factors:

- the amount of GST collected by the Commonwealth (the national GST pool);
- Victoria's GST relativity; and
- Victoria's share of the national population.

### *National GST pool*

If consumption growth or dwelling investment recover slower than expected, the national GST pool could grow at a slower pace, resulting in lower GST grants to Victoria. Movements in the household savings ratio and changes to household consumption behaviour are also sources for uncertainty for the GST pool outlook. Over the forward estimates, slower than expected growth in the national population poses a downside risk to the levels of aggregate consumer spending.

### *GST relativities*

The national GST pool is shared between states and territories based on relativities determined annually by the Commonwealth Treasurer, informed by the recommendations of the Commonwealth Grants Commission.

These relativities are based on the relative fiscal capacity of each jurisdiction and are influenced by differences in revenue bases and costs of delivering services. Relativities are sensitive to a broad range of factors, including demographics, infrastructure needs, developments in property markets and global commodity prices (particularly for iron ore and coal).

### *Population*

Restrictions on overseas migration may further impact Victoria's population growth relative to the other states and territories, resulting in a decrease in Victoria's share of the national population. If Victoria's population growth is higher than forecast compared with other states, Victoria's share of GST revenue could increase. Conversely, should other states have higher population growth than expected compared with Victoria this would negatively affect Victoria's GST revenue.

### ***Commonwealth no-worse off guarantee for GST entitlement***

In 2018, the Commonwealth changed the system of horizontal fiscal equalisation (HFE), which introduced:

- a minimum GST revenue sharing relativity (relativity floor) of 0.70 commencing in 2021-22 and rising to 0.75 from 2024-25;
- a small boost to the GST revenue pool from 2021-22 with additional Commonwealth financial assistance; and
- the transition of the HFE system from full equalisation (so-called equalising to the strongest state) to ‘reasonable’ equalisation, based upon the fiscal capacity of the stronger of New South Wales or Victoria.

During a six-year transition period commencing in 2021-22, each state or territory is entitled to receive additional Commonwealth financial assistance to ensure it is no worse off compared to its GST entitlement had full equalisation been maintained. The no-worse-off guarantee is currently legislated until the end of the transition period in 2026-27, which poses a fiscal risk to states and territories. Modelling the potential impact of the removal of the no-worse-off guarantee is presented in Budget Paper No. 5, Chapter 4 *State Revenue* Box 4.3 *Impacts of the new GST distribution system*.

As part of the reforms, the Productivity Commission is required to review the changed distribution system by 2026 to ensure the updated system is operating efficiently, effectively and as intended. Victoria will continue to work with other state governments and the Commonwealth to ensure Victoria receives its fair share of GST.

### **National Skills Agreement**

In July 2020, the Commonwealth and the states agreed to negotiate a new National Skills Agreement (NSA) to replace the existing National Agreement for Skills and Workforce Development. The Commonwealth expects to finalise a new NSA by August 2021, with a transition period commencing from 1 January 2022. The quantum and conditions of funding are dependent on ongoing negotiations between the Commonwealth and states. Conditions of the current proposed Agreement may increase fiscal and policy risks to the State.

## CHAPTER 5 – POSITION AND OUTLOOK OF THE BROADER PUBLIC SECTOR

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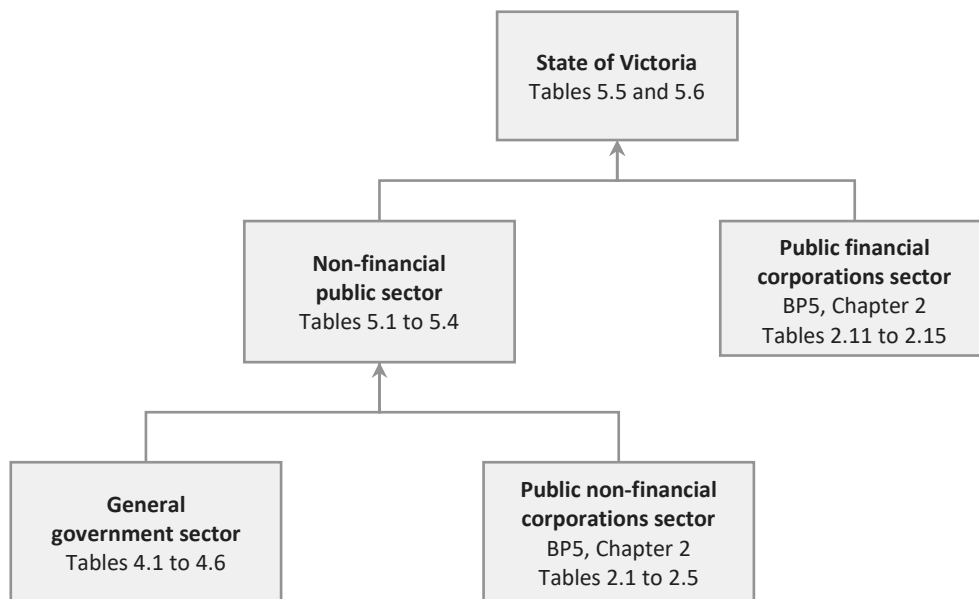
- The State of Victoria’s net result from transactions is projected to improve from a deficit of \$17.4 billion in 2021-22 to a deficit of \$8.5 billion in 2024-25, with an average deficit of \$11.0 billion over the budget and forward estimates.
- The net result from transactions of the non-financial public sector (NFPS) is expected to improve from a deficit of \$12.6 billion in 2021-22 to a deficit of \$3.3 billion by 2024-25. This improvement is primarily driven by the general government sector, for which revenues are growing faster than expenses over the budget and forward estimates.
- NFPS net debt, which includes both general government and public non-financial corporation (PNFC) sectors, as a proportion of gross state product (GSP) is estimated to average 28.1 per cent over the budget and forward estimates. This is consistent with the Government’s fiscal strategy.
- The net result from transactions of the PNFC sector is anticipated to be an average surplus of \$268 million a year over the budget and forward estimates, while the average operating cash flow surplus is expected to be \$1.7 billion a year over this period once non-cash items such as depreciation are removed.
- The net result from transactions of the public financial corporations (PFC) sector is forecast to deteriorate over the budget and forward estimates from a deficit of \$4.6 billion in 2021-22 to a deficit of \$5.2 billion by 2024-25. The average operating cash flow surplus of the PFC sector over this period is \$250 million a year.

This chapter provides an overview of the activities of the broader public sector, comprising:

- the NFPS, which consolidates the general government and the PNFC sectors. The general government sector is discussed in Chapter 4 *Budget Position and Outlook*. The PNFC sector comprises a wide range of entities that provide services that are primarily funded by user charges and fees. The main services provided by PNFCs include water, housing, and transport services; and
- the State of Victoria, which consolidates the NFPS and the PFC sectors. PFCs can be categorised into two broad types: those that provide services to the general public and businesses (such as WorkSafe Victoria, the Transport Accident Commission and State Trustees Limited), and those that provide financial services, predominantly to other government entities (such as the Victorian Funds Management Corporation, Treasury Corporation of Victoria and the Victorian Managed Insurance Authority).

This chapter comments on each of the sectors but includes tables with data for the State of Victoria and the NFPS only. The equivalent information for the PFC and PNFC sectors can be found in Budget Paper No. 5, Chapter 2 *Supplementary Uniform Presentation Framework Tables*.

The following chart shows the relationship between the various sectors of the State and indicates the relevant tables that disclose the data on these sectors within this budget paper and Budget Paper No. 5 *Statement of Finances*.



## NON-FINANCIAL PUBLIC SECTOR

The net result from transactions of the NFPS is forecast to be a deficit of \$12.6 billion in 2021-22 with this then improving to a deficit of \$3.3 billion in 2024-25. This improvement is largely driven by the general government sector for which the net result from transactions is forecast to improve from a deficit of \$11.6 billion in 2021-22 to a deficit of \$2.1 billion in 2024-25.

Please note that the general government sector and PNFC sector results may not equal the results shown for the NFPS due to inter-sector transfers.

**Table 5.1: Summary operating statement for the non-financial public sector <sup>(a)</sup> (\$ million)**

	2019-20 actual	2020-21 revised	2021-22 budget	2022-23 estimate	2023-24 estimate	2024-25 estimate
<b>Revenue and income from transactions</b>						
Taxation	22 745	23 033	26 127	28 602	30 583	32 130
Dividends, income tax equivalent and interest <sup>(b)</sup>	382	369	480	403	404	415
Sales of goods and services	11 769	11 462	12 531	13 434	13 577	13 755
Grants	32 772	35 744	36 767	39 689	40 523	41 516
Other revenue and income	3 427	3 550	4 194	4 005	3 882	4 014
<b>Total revenue and income from transactions</b>	<b>71 095</b>	<b>74 157</b>	<b>80 100</b>	<b>86 134</b>	<b>88 969</b>	<b>91 831</b>
<i>% change</i>	-2.7	4.3	8.0	7.5	3.3	3.2
<b>Expenses from transactions</b>						
Employee expenses	28 597	30 615	33 155	34 039	35 027	35 770
Superannuation <sup>(c)</sup>	3 621	3 762	4 387	4 428	4 511	4 589
Depreciation	6 395	6 865	7 174	7 557	7 983	8 643
Interest expense	2 761	3 229	3 456	3 918	4 494	5 207
Grant expense	11 260	16 883	15 441	13 570	13 360	13 604
Other operating expenses	25 560	31 286	29 115	27 400	26 891	27 316
<b>Total expenses from transactions</b>	<b>78 194</b>	<b>92 639</b>	<b>92 728</b>	<b>90 912</b>	<b>92 264</b>	<b>95 128</b>
<i>% change</i>	7.7	18.5	0.1	-2.0	1.5	3.1
<b>Net result from transactions</b>	<b>(7 099)</b>	<b>(18 481)</b>	<b>(12 628)</b>	<b>(4 778)</b>	<b>(3 295)</b>	<b>(3 297)</b>
Total other economic flows included in net result	(3 357)	(840)	(501)	(467)	39	(429)
<b>Net result</b>	<b>(10 456)</b>	<b>(19 321)</b>	<b>(13 129)</b>	<b>(5 246)</b>	<b>(3 256)</b>	<b>(3 727)</b>

Source: Department of Treasury and Finance

Notes:

(a) This is a summary operating statement. The comprehensive operating statement is presented in Budget Paper No. 5 Statement of Finances. Figures in this table are subject to rounding to the nearest million and may not add up to totals.

(b) Comprises dividends, income tax and rate equivalent revenue and interest.

(c) Comprises superannuation interest expense and other superannuation expenses.

The net result from transactions of the PNFC sector is projected to improve from a surplus of \$82 million in 2021-22 to a surplus of \$361 million in 2024-25. The most significant improvement is expected to occur in 2022-23, as revenues are expected to return to pre-coronavirus (COVID-19) pandemic levels.

Over this period metropolitan water authorities are projected to report an average surplus of \$297 million a year. In contrast, Homes Victoria is projected to report an average deficit of \$37 million a year, although it maintains a net operating cash flow surplus (see below). Overall, the net result from transactions of the PNFC sector is projected to average an annual surplus of \$268 million over the budget and forward estimates.

## Application of cash resources

Table 5.2 shows the net cash flows from operating activities of the NFPS is projected to increase from a deficit of \$876 million in 2021-22 to a surplus of \$4.6 billion by 2024-25. On average, net cash flows from operating activities funds 11.5 per cent of the projected net investment in fixed assets with the remainder being funded largely by borrowings.

Homes Victoria is projected to generate a net operating cash flow surplus averaging \$207 million a year over the budget and forward estimates. This cash flow surplus indicates that Homes Victoria remains in a financially sustainable position despite the net result from transactions deficit noted above which primarily relates to non-cash expenses such as depreciation. The PNFC sector overall is projected to record an average operating cash flow surplus of \$1.7 billion a year over the budget and forward estimates once non-cash items such as depreciation are removed.

**Table 5.2: Application of cash resources for the non-financial public sector<sup>(a)</sup> (\$ million)**

	2019-20 actual <sup>(b)</sup>	2020-21 revised	2021-22 budget	2022-23 estimate	2023-24 estimate	2024-25 estimate
Net result from transactions	(7 099)	(18 481)	(12 628)	(4 778)	(3 295)	(3 297)
Add back: operating cash flows not recognised in the net operating balance <sup>(c)</sup>	5 549	2 187	11 752	7 491	7 180	7 935
<b>Net cash flows from operating activities</b>	<b>(1 550)</b>	<b>(16 294)</b>	<b>(876)</b>	<b>2 713</b>	<b>3 885</b>	<b>4 638</b>
<b>Less: Total net investment in fixed assets<sup>(d)</sup></b>	<b>12 133</b>	<b>15 639</b>	<b>22 902</b>	<b>21 271</b>	<b>22 420</b>	<b>23 307</b>
<b>Surplus/(deficit) of cash from operations after funding net investments in fixed assets</b>	<b>(13 683)</b>	<b>(31 933)</b>	<b>(23 778)</b>	<b>(18 558)</b>	<b>(18 535)</b>	<b>(18 670)</b>
Less:						
Leases and service concession arrangements <sup>(e)</sup>	2 289	3 415	3 573	2 451	1 918	928
Other movements	3 936	(32)	(107)	(57)	(89)	(117)
<b>Decrease/(increase) in net debt</b>	<b>(19 908)</b>	<b>(35 317)</b>	<b>(27 243)</b>	<b>(20 952)</b>	<b>(20 363)</b>	<b>(19 480)</b>

Source: Department of Treasury and Finance

Notes:

- (a) Figures in this table are subject to rounding to the nearest million and may not add up to totals.
- (b) Movements in 2019-20 include the impact of new accounting standards.
- (c) Includes depreciation, prepayments and movements in the superannuation liability and liability of employee benefits, and the progressive unwinding of the grant of a right to the operator liability.
- (d) Includes total purchases of plant, property and equipment, and capital contributions to other sectors of government net of proceeds from asset sales.
- (e) Includes most operating leases which are now required to be recognised as lease liabilities. It also includes the financial liabilities relating to public private partnerships including the High Capacity Metro Trains Project, the Metro Tunnel, the new Footscray Hospital, the Frankston Hospital Redevelopment, the North East Link and the Western Roads Upgrade.

## Infrastructure

Table 5.2 also provides estimates of the net investment in non-financial assets which represents the difference between infrastructure expenditure and the proceeds from asset sales. The total net investment in non-financial assets by the NFPS is projected to average \$22.4 billion a year over the budget and forward estimates.

The main PNFC sector infrastructure projects under development are:

- investment in transport infrastructure and rolling stock to meet patronage growth and improve network performance. This includes the new metropolitan trains, Next Generation Trams, tram infrastructure upgrades and maintenance facilities for rolling stock; and
- various water and sewer related infrastructure projects, such as the Western Treatment Plant Primary Treatment Augmentation, the Lockerbie Main Sewer, the Western Irrigation Network Project and the modernisation of various irrigation systems by Southern Rural Water.

Further details on these projects is contained in Budget Paper No. 4, Chapter 3 *Public non-financial corporations capital program*.

## Non-financial public sector net debt and net financial liabilities

Table 5.3 details the NFPS net debt and superannuation liabilities. It shows that net debt is expected to increase from \$95.3 billion at 30 June 2021 to \$183.3 billion by 30 June 2025. NFPS net debt as a proportion of GSP averages 28.1 per cent over the budget and forward estimates. The increase in net debt is predominately due to additional borrowings required by the general government sector to fund the Government's response to the coronavirus (COVID-19) pandemic. General government sector net debt as a proportion of GSP averages 23.7 per cent over the budget and forward estimates.

Superannuation liabilities are projected to fall over the budget and forward estimates due mainly to the annual budget contributions that are being made as part of the Government's commitment to fully fund the unfunded superannuation liability by 2035.

Overall, the net financial liabilities to GSP ratio is projected to increase from 32.5 per cent in 2020-21 to 41.3 per cent in 2024-25.

**Table 5.3: Non-financial public sector net debt and net financial liabilities <sup>(a)</sup> (\$ billion)**

	2019-20 actual	2020-21 revised	2021-22 budget	2022-23 estimate	2023-24 estimate	2024-25 estimate
<b>Assets</b>						
Cash and deposits	14.6	14.9	15.0	15.2	15.7	16.0
Advances paid	0.5	0.7	0.8	0.8	0.9	1.0
Investments, loans and placements	3.2	1.7	1.5	1.7	2.0	2.4
<b>Total</b>	<b>18.3</b>	<b>17.2</b>	<b>17.3</b>	<b>17.7</b>	<b>18.6</b>	<b>19.3</b>
<b>Liabilities</b>						
Deposits held and advances received	1.7	1.7	1.6	1.6	1.6	1.6
Borrowings	76.6	110.9	138.3	159.6	180.8	201.1
<b>Total</b>	<b>78.2</b>	<b>112.5</b>	<b>139.8</b>	<b>161.2</b>	<b>182.4</b>	<b>202.6</b>
<b>Net debt <sup>(b)</sup></b>	<b>60.0</b>	<b>95.3</b>	<b>122.5</b>	<b>143.5</b>	<b>163.8</b>	<b>183.3</b>
Superannuation liability	31.3	28.8	28.1	27.3	26.5	25.7
<b>Net debt plus superannuation liability</b>	<b>91.3</b>	<b>124.1</b>	<b>150.6</b>	<b>170.8</b>	<b>190.3</b>	<b>209.0</b>
Other liabilities (net) <sup>(c)</sup>	30.0	27.2	32.4	32.6	32.6	31.8
<b>Net financial liabilities <sup>(d)</sup></b>	<b>121.3</b>	<b>151.4</b>	<b>183.0</b>	<b>203.3</b>	<b>222.9</b>	<b>240.8</b>
	<i>(per cent)</i>					
Net debt to GSP <sup>(e)</sup>	12.8	20.5	24.3	27.1	29.5	31.5
Net debt plus superannuation liability to GSP <sup>(e)</sup>	19.5	26.7	29.9	32.3	34.3	35.9
Net financial liabilities to GSP <sup>(e)</sup>	25.9	32.5	36.3	38.5	40.2	41.3
Net debt plus superannuation liability to revenue <sup>(f)</sup>	128.4	167.4	188.0	198.3	213.9	227.6

Source: Department of Treasury and Finance

Notes:

- (a) Figures in this table are subject to rounding to the nearest million and may not add up to totals.
- (b) Net debt is the sum of borrowings, deposits held and advances received less the sum of cash and deposits, advances paid, and investments, loans and placements. Movements in 2019-20 include the impact of the new accounting standards. Further information on the impact of these can be found at Note 1.7.2 of Budget Paper No. 5, Chapter 1 Estimated Financial Statements for the general government sector.
- (c) Other liabilities include other employee entitlements and provisions and other non-equity liabilities, less other non-equity financial assets.
- (d) Net financial liabilities is total liabilities less financial assets (excluding investments in other sector entities).
- (e) The ratios to GSP may vary from publications year to year due to revisions to the Australian Bureau of Statistics GSP data.
- (f) The sum of NFPS net debt (excluding advances paid) plus the superannuation liability as a proportion of NFPS total operating revenue.

Table 5.4 projects several indicators of financial sustainability for the NFPS over the budget and forward estimates.

The operating cash flow surplus to revenue ratio is an indication of the extent to which the cash generated from operations can be used to fund infrastructure. This ratio increases strongly from negative 1.1 per cent in 2021-22 to positive 5.1 per cent by 2024-25 due to successive increases in the operating cash flow surplus over the budget and forward estimates. These increases reflect a first step in the re-alignment of revenue and expenditure, driven by the combined impact of increased revenue associated with the economic recovery, the tapering of targeted, short-term expenditure that supported Victorians during public health restrictions and the implementation of savings and efficiencies to improve the effectiveness of departmental spending.



The ratio of gross debt to revenue, which indicates the overall debt burden, is estimated to be 174.6 per cent in 2021-22. The NFPS interest expense to revenue ratio is a measure of the State's debt service burden. This ratio increases in 2021-22 in line with the increased debt but is expected to remain manageable at an average of 4.9 per cent a year over the budget and forward estimates. This is well below the levels seen during the 1990s.

**Table 5.4: Indicators of financial sustainability for the non-financial public sector** (per cent)

	2019-20 <i>actual</i>	2020-21 <i>revised</i>	2021-22 <i>budget</i>	2022-23 <i>estimate</i>	2023-24 <i>estimate</i>	2024-25 <i>estimate</i>
Operating cash flow surplus / (deficit) to revenue	(2.2)	(22.0)	(1.1)	3.1	4.4	5.1
Gross debt to revenue <sup>(a)</sup>	110.1	151.7	174.6	187.2	205.0	220.7
Interest expense to revenue	3.9	4.4	4.3	4.5	5.1	5.7

Source: Department of Treasury and Finance

Note:

(a) Gross debt includes borrowings, deposits held and advances received.

## STATE OF VICTORIA

Table 5.5 shows the operating results for the State. The net result from transactions is projected to improve from a deficit of \$17.4 billion in 2021-22 to a deficit of \$8.5 billion in 2024-25, with an average deficit of \$11.0 billion over the budget and forward estimates. This improvement is primarily due to revenues growing faster than expenses over the forward estimates, driven by movements in the general government sector which are explained in chapter 4.

The net result from transactions excludes other economic flows such as projected capital gains on the investments that are held by the State's insurance agencies to meet these agencies' liabilities. Other economic flows are projected to average \$1.5 billion a year over the budget and forward estimates.

When other economic flows are included, the State's net result improves from a deficit of \$16.3 billion in 2021-22 to a deficit of \$6.8 billion in 2024-25, with an average deficit of \$9.5 billion a year over the budget and forward estimates. In 2020-21, other economic flows are expected to be lower than they are across the budget and forward estimates. This is largely due to unfavourable insurance claims experience in 2020-21 offsetting the favourable impacts of strong investment returns and increases in the bond rates that underlie the valuation of insurance liabilities.

**Table 5.5: Operating results – State of Victoria <sup>(a)</sup>** (\$ million)

	2019-20 actual	2020-21 revised	2021-22 budget	2022-23 estimate	2023-24 estimate	2024-25 estimate
<b>Revenue and income from transactions</b>						
Taxation	22 730	23 014	26 110	28 585	30 565	32 112
Dividends and interest <sup>(b)</sup>	2 836	2 124	1 829	1 809	2 346	2 432
Sales of goods and services	15 810	15 843	16 936	17 988	18 294	18 665
Grants	32 505	35 435	36 008	39 005	39 576	40 648
Other revenue and income	3 447	3 575	4 220	4 031	3 908	4 041
<b>Total revenue and income from transactions</b>	<b>77 327</b>	<b>79 991</b>	<b>85 102</b>	<b>91 418</b>	<b>94 690</b>	<b>97 899</b>
% change	-1.7	3.4	6.4	7.4	3.6	3.4
<b>Expenses from transactions</b>						
Employee expenses	28 503	30 611	33 122	34 016	35 010	35 754
Superannuation <sup>(c)</sup>	3 653	3 799	4 424	4 467	4 551	4 630
Depreciation	6 467	6 947	7 277	7 667	8 098	8 759
Interest expense	3 002	3 117	3 430	3 899	4 474	5 182
Grant expense	11 276	16 344	15 260	13 378	13 166	13 411
Other operating expenses	33 447	40 067	38 981	37 780	37 742	38 659
<b>Total expenses from transactions</b>	<b>86 348</b>	<b>100 884</b>	<b>102 494</b>	<b>101 208</b>	<b>103 041</b>	<b>106 395</b>
% change	7.4	16.8	1.6	-1.3	1.8	3.3
<b>Net result from transactions</b>	<b>(9 021)</b>	<b>(20 893)</b>	<b>(17 392)</b>	<b>(9 790)</b>	<b>(8 351)</b>	<b>(8 496)</b>
Total other economic flows included in net result	(6 677)	238	1 055	1 140	2 035	1 654
<b>Net result</b>	<b>(15 699)</b>	<b>(20 655)</b>	<b>(16 337)</b>	<b>(8 650)</b>	<b>(6 316)</b>	<b>(6 842)</b>

Source: Department of Treasury and Finance

Notes:

- (a) This is a summary operating statement. The comprehensive operating statement is presented in Budget Paper No. 5 Statement of Finances. Figures in this table are subject to rounding to the nearest million and may not add up to totals.
- (b) Comprises dividends and interest.
- (c) Comprises superannuation interest expense and other superannuation expenses.

The whole of State result is mainly driven by the NFPS, but includes the PFC sector which is forecast to report an average net result from transactions deficit of \$4.9 billion a year over the budget and forward estimates.

Other economic flows, which largely relate to projected capital gains on insurance investments and movements in deferred tax assets, are expected to average \$2.7 billion a year over the budget and forward estimates. When these are included, the average net result for the PFC sector is a deficit of \$2.3 billion a year over the budget and forward estimates.

Table 5.6 shows the State's net assets are projected to decrease over the budget and forward estimates from \$163.2 billion in 2020-21 to \$154.1 billion by 2024-25. While total assets are expected to increase over the budget and forward estimates, this increase is more than offset by higher liabilities, largely due to increased borrowings.

In particular, financial assets are estimated to increase from \$73.8 billion in 2020-21 to \$77.9 billion by 2024-25 and non-financial assets, including infrastructure, are estimated to increase from \$330.6 billion in 2020-21 to \$423.6 billion by 2024-25.

The superannuation liability is projected to fall from \$28.8 billion in 2020-21 to \$25.7 billion in 2024-25 reflecting the contributions the Government is making to fully fund the liabilities of the former State Superannuation Fund by 2035.

As noted above, these favourable movements are more than offset by a projected increase in borrowings from \$124.0 billion in 2020-21 to \$214.3 billion by 2024-25. Other liabilities are also projected to increase from \$86.6 billion in 2020-21 to \$105.8 billion by 2024-25 largely due to growth in the value of the outstanding claims liabilities reported by the State's insurance agencies.

**Table 5.6: Financial position of the State of Victoria <sup>(a)</sup> (\$ billion)**

	2019-20 <i>actual</i>	2020-21 <i>revised</i>	2021-22 <i>budget</i>	2022-23 <i>estimate</i>	2023-24 <i>estimate</i>	2024-25 <i>estimate</i>
<b>Assets</b>						
Total financial assets <sup>(b)</sup>	69.1	73.8	72.6	73.6	75.7	77.9
Total non-financial assets <sup>(c)</sup>	315.4	330.6	351.0	374.4	398.0	423.6
<b>Total assets</b>	<b>384.5</b>	<b>404.4</b>	<b>423.5</b>	<b>447.9</b>	<b>473.7</b>	<b>501.5</b>
<b>Liabilities</b>						
Superannuation	31.3	28.8	28.1	27.3	26.5	25.7
Borrowings	87.8	124.0	151.5	172.9	194.1	214.3
Deposits held and advances received	1.7	1.7	1.6	1.6	1.6	1.6
Other liabilities <sup>(d)</sup>	84.3	86.6	93.7	97.8	102.1	105.8
<b>Total liabilities</b>	<b>205.0</b>	<b>241.2</b>	<b>274.8</b>	<b>299.6</b>	<b>324.2</b>	<b>347.4</b>
<b>Net assets</b>	<b>179.5</b>	<b>163.2</b>	<b>148.7</b>	<b>148.4</b>	<b>149.5</b>	<b>154.1</b>

Source: Department of Treasury and Finance

Notes:

- (a) Figures in this table are subject to rounding to the nearest million and may not add up to totals.
- (b) Financial assets include cash and deposits, advances paid, investments, loans and placements, receivables, and investments accounted for using the equity method.
- (c) Non-financial assets include inventories, non-financial assets held for sale, land, buildings, infrastructure, plant and equipment, and other non-financial assets.
- (d) Other liabilities consist of payables, employee benefits and other provisions.



## APPENDIX A – SENSITIVITY ANALYSIS

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The *2021-22 Budget* relies on forecasts and judgements about the economic and financial conditions for the Victorian general government sector. Uncertainty in these conditions, for example as a result of international developments and other risks to the national economy, may cause the actual results to differ from projections.

This sensitivity analysis explores the impact of variations in the macroeconomic outlook on key fiscal aggregates of the general government sector using two alternative approaches.

The first approach quantifies the fiscal impacts of a scenario involving simultaneous variations in economic parameters that represent key risks to the economic outlook described in Chapter 2 *Economic Context*. This scenario was selected to cover a plausible shock that could affect Victoria over the budget and forward estimates period, and the modelling takes account of linkages between key international, Australian and Victorian economic aggregates.

The modelled outcomes are intended to be used as a guide and care should be exercised in interpreting the results. In particular, economic shocks tend to be idiosyncratic in nature, with the modelled scenario unlikely to completely reflect any future shock that could occur. Departures from this scenario would likely result in different impacts on the budget. Furthermore, the modelled results of the shocks do not incorporate any policy responses to the shocks and their subsequent effects on the economic outlook.

The second approach considers the fiscal impacts of independent variations in major economic parameters, holding constant all parameters other than the indicator of interest. This analysis may be useful for assessing the impact on fiscal aggregates of a forecast error in a single economic parameter. In practice, economic variations rarely occur in isolation, and a modelled scenario is likely to be more appropriate to illustrate the fiscal impacts of an economic environment materially different from that presented in the budget papers.

## FISCAL IMPACTS OF VARIATIONS TO THE ECONOMIC OUTLOOK

This part of the sensitivity analysis quantifies a key risk identified in Chapter 2 *Economic Context* and presents how this risk might affect the State's economic outlook and fiscal aggregates.

The scenario considered is a significant delay to the global roll-out of effective coronavirus (COVID-19) vaccines, including among Victoria's key trading partners. This leads to further outbreaks of COVID-19 and restrictions in major economies outside Australia, slowing the global economic recovery.

The economic impacts of the scenario have been modelled using VURMTAX, a computable general equilibrium model developed by Victoria University's Centre of Policy Studies. The results of the scenario are analysed as a deviation from the 'business as usual' base case, which represents the economic forecasts outlined in Chapter 2 *Economic Context*.

The changes in economic variables resulting from the modelled shocks are then mapped into estimated revenue and expenditure impacts using elasticities that describe the historical relationship between fiscal outcomes and major macroeconomic parameters. These fiscal impacts are presented in Table A.2.<sup>1</sup>

### Scenario: A protracted global recovery

The global coronavirus (COVID-19) pandemic has had a significant impact on the global economy. Even with the global recovery underway, there remains a high degree of uncertainty around the economic outlook. Key to the global recovery is the future path of virus transmissions across the globe, and relatedly the speed and efficacy of the global vaccine roll-out. This scenario explores a delay to the effective global roll-out of vaccines, leading to renewed outbreaks and restrictions in major economies outside Australia, and lower confidence domestically.

The pandemic and the international responses to contain it led to a deep and synchronised contraction in the global economy. The global economy shrank by 3.3 per cent in 2020, the largest fall in global output since the Great Depression.

Many countries have had success in slowing the spread of the virus, which has generally been associated with better economic outcomes. Success in reducing case numbers allowed restrictions to be eased, and economic activity to pick up. Global economic activity picked up significantly in the September quarter 2020 as economies bounced back from low levels, and recovered further in the December quarter.

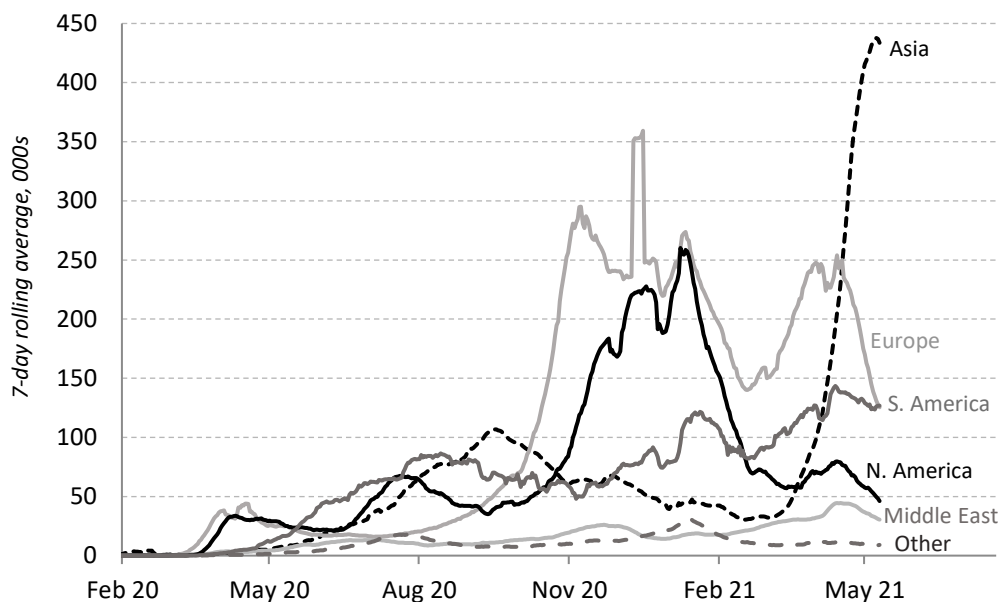
However, the future path of COVID-19 remains a key uncertainty for the global economy's ongoing recovery. While many countries had initial success in reducing the spread of the virus, some continue to face renewed outbreaks, prompting authorities to reimpose restrictions. In April, global weekly case numbers surpassed peaks seen in 2020.

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<sup>1</sup> The Department of Treasury and Finance maintains a set of elasticities estimating the relationships between major economic parameters and revenue and expenditure lines, including superannuation, and dividends and income tax equivalents from the public financial and non-financial corporations.

Case numbers in the United States, the region with the highest number of cumulative cases, declined in early 2021, but renewed outbreaks over March in Europe, Asia and parts of South America have kept global daily case numbers elevated (Chart A.1). Case numbers in France, Germany, Turkey and Poland rose sharply over March, prompting the reimposition of restrictions. At the same time, Brazil’s case numbers reached record levels, and in India case numbers surged. These renewed outbreaks emphasise the ongoing uncertainty associated with the path of COVID-19 until vaccines are widely rolled out.

**Chart A.1: Daily COVID-19 case numbers**

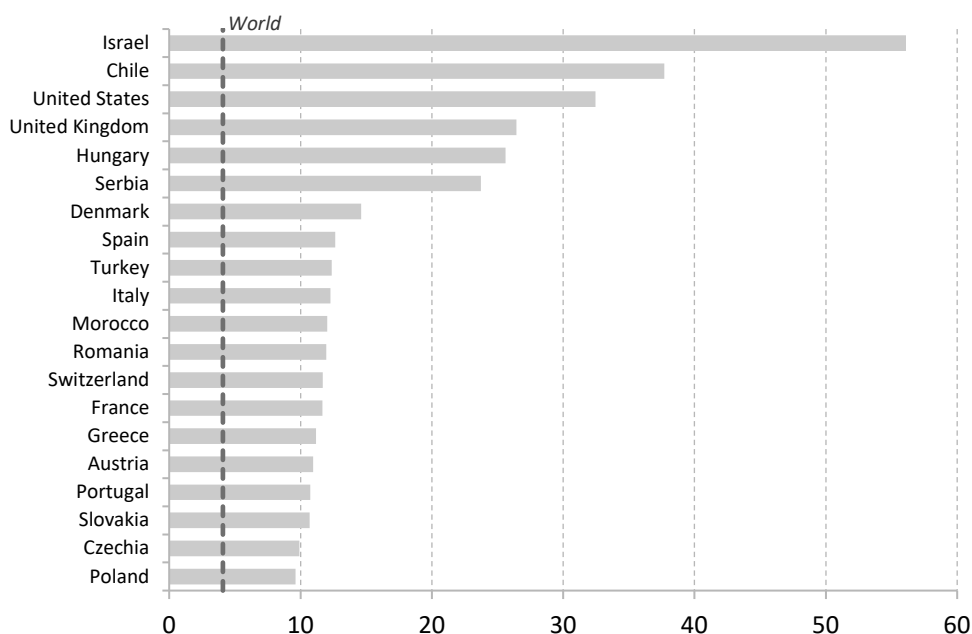


Sources: Johns Hopkins University; Department of Treasury and Finance.

The successful vaccination of the global population is another key uncertainty. Many countries have begun the roll-out of various vaccines, but with less than 5 per cent of the global population fully vaccinated, there is much further to go. While some countries have delivered a large number of vaccines to the population, the share of the population that is fully vaccinated (those that have received a full vaccine course, which needs two separate injections for some vaccines) remains low in most countries (Chart A.2).

The roll-out of vaccines has already faced several hurdles, with progress on the production and distribution of vaccines mixed. Some countries, such as the United States, Israel and the United Kingdom, have made rapid progress inoculating the population, while some countries, particularly in Europe, are behind planned vaccination milestones. Delays to the production of some vaccines have slowed the roll-out, while restrictions on vaccine exports have hindered progress for some countries. Concerns about vaccine side-effects caused some countries to pause or restrict their vaccine programs, although generally pauses were temporary. Further complicating the roll-out is the spread of variants of the COVID-19 virus, and the uncertainty surrounding the efficacy of the vaccine against these emerging strains of the virus. These factors contribute to the elevated uncertainty surrounding the successful inoculation of the global population.

**Chart A.2: Share of total population fully vaccinated (top 20 countries)**



Sources: Johns Hopkins University; Department of Treasury and Finance.

Note: A fully vaccinated person has received all required doses of a vaccine. Chart shows those countries with a population greater than 5 million as of 2000.

Consistent with the outlook presented in the International Monetary Fund’s (IMF) April 2021 *World Economic Outlook*, the base case assumes the global economy will grow by 6.0 per cent in 2021, taking the global economy above pre-coronavirus (COVID-19) levels, and by a further 4.4 per cent in 2022.

In the alternative economic scenario modelled here, a delay to the effective global roll-out of vaccines leads to renewed outbreaks and restrictions in major economies outside Australia, which slows the global economic recovery.



Global growth is assumed to be 1.6 percentage points lower than the baseline in 2021 as countries reintroduce or delay the easing of health restrictions in the face of entrenched virus variants and growing case numbers, thereby restricting economic activity.<sup>2</sup>

The gradual increases in migrants, students and tourists expected in the base case are assumed to be delayed by a further six months due to the delay in the effective global roll-out of vaccines. This defers the recovery in Australia and Victoria's service exports – in particular, education exports and international tourism.

International education made \$13.7 billion in revenue for the Victorian economy in 2019. In the scenario modelled, the delayed return of international students has a significant impact on Victoria's education exports.

International tourism, which accounted for 1.0 per cent of Victorian gross value added in 2019-20, also experiences a further delayed recovery in this scenario.

Overall, in the scenario, the delayed return of students and tourists results in a 13 per cent fall in Victoria's total service exports relative to the base case in 2022.

International migration has been a key driver of Victoria's population growth and economic growth over the few years leading up to the pandemic. In the scenario modelled, the population is smaller than in the base case, due to the delayed return of overseas migration to more normal levels.

Aside from these direct effects on the Victorian economy, lower levels of global growth and the extended constraints on international people movements weigh heavily on domestic business confidence. This causes businesses in Victoria and other states to put off investment decisions. Lower business investment, relative to the base case, is a significant driver of the lower level of Victorian economic activity.

The shocks to trade, overseas migration and business confidence reduce Victoria's gross state product (GSP) by a peak of about 1.0 per cent in 2022-23 and by 0.9 per cent by 2024-25, compared with the base case.

Dwelling investment is also lower, as weaker domestic activity drags on house prices, but remains less affected than business investment. Total investment, including business investment and dwelling investment, is around 2.6 per cent lower by 2024-25.

Lower domestic economic activity weighs on demand for labour, and employment growth is about 0.9 per cent lower in 2022-23. A lower supply of workers – with Victoria's population about 0.9 per cent smaller by 2024-25 due to lower international migration – means that employment is still 0.8 per cent lower than the base case by 2024-25.

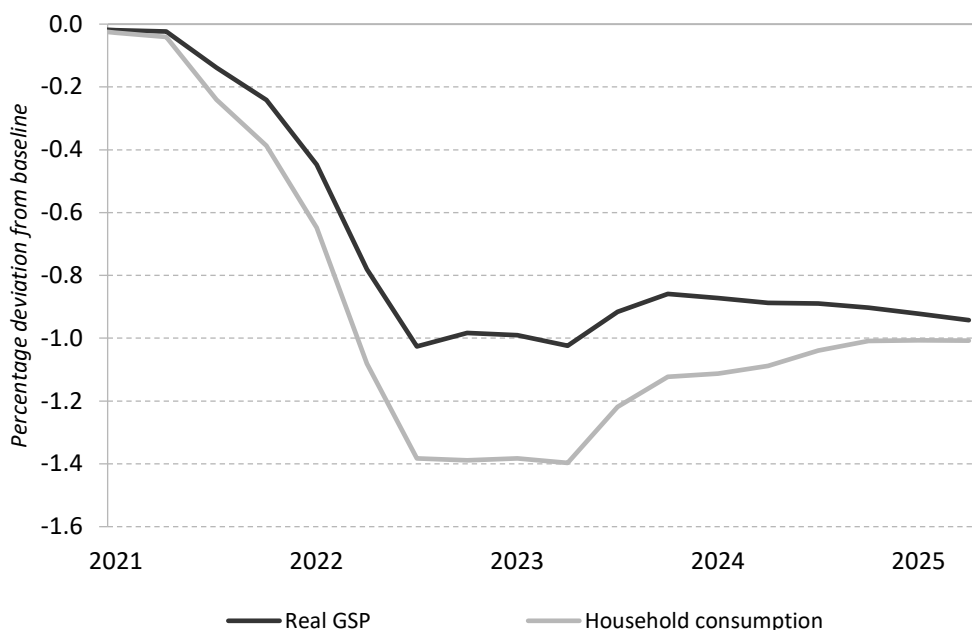
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<sup>2</sup>This size of the deviation in global economic growth is consistent with the downside scenario in the IMF's April 2021 *World Economic Outlook*.

Lower employment levels reduce household income which, along with a lower population, weigh on household consumption. Under this scenario, consumption is forecast to be around 1.4 per cent lower in 2022-23. As migrant, student and tourism numbers start to gradually rise and business confidence and investment improve, consumption also picks up, but remains 1.0 per cent lower than the base line by 2024-25. The negative impact on household consumption is exacerbated by a rise in the savings rate, as households save some of the funds they would have otherwise spent on international tourism, rather than spend the full amount domestically.

Government consumption is also lower over the forecast period as a lower population needs a lower level of expenditure. In the scenario there is no further discretionary fiscal expenditure in response to the shock.

**Chart A.3: Scenario impact on select variables**



Weaker domestic activity puts downward pressure on the real exchange rate, leading to a depreciation of the domestic currency against other currencies. The lower exchange rate increases the international competitiveness of domestic exporters. This raises goods export volumes relative to the baseline, more than offsetting the low service exports in the scenario.

The depreciation of the domestic currency raises the cost of imports to households, placing upward pressure on consumer prices. This is more than offset, though, by weaker domestic activity, with the net effect that consumer prices are lower in the scenario.

Table A.1 summarises the economic effects of a slow global realisation of the benefits of vaccines.

**Table A.1: Projected economic impact of a protracted global recovery <sup>(a)</sup> (per cent)**

	2021-22	2022-23	2023-24	2024-25
	estimate	estimate	estimate	estimate
Real GSP	(0.40)	(1.01)	(0.88)	(0.91)
Employment	(0.38)	(0.87)	(0.77)	(0.82)
Consumer price index <sup>(b)</sup>	(0.20)	(0.40)	(0.32)	(0.30)
Wage price index	(0.25)	(0.61)	(0.50)	(0.39)

Source: Department of Treasury and Finance

Notes:

(a) Figures reported are the change in the level of each parameter relative to the baseline forecasts as presented in Chapter 2 Economic Context.

(b) In this simulation the GDP deflator is the reference price variable.

The scenario has a negative impact on the Victorian Government's fiscal position (Table A.2). Lower levels of domestic activity and slower population growth weigh on property market activity, which lowers property-related taxation revenue, including land transfer duty and land taxes. Lower household consumption leads to a smaller national goods and services tax (GST) pool and so lower GST grants revenue. The decline in employment also leads to lower payroll tax revenue. As a result of these revenue effects, income from transactions is lower over the forward estimates.

Expenses are also lower in the scenario, although the net impact on total transactions is negative. Lower employment levels reduce employee entitlements. The magnitude of the decrease is larger towards the end of the forward estimates, which reflects a lag in public sector wages adjusting to changes in private sector wages. These impacts reflect the assumed relationship between private and public sector employment and wages in the model; namely that public sector employment is a fixed share of overall employment, and public sector wage growth corresponds to private sector wage growth. Service delivery expenses are a little lower because of lower consumer prices. Overall, the net impact on the Government's fiscal position is negative.

**Table A.2: Projected fiscal impact of a protracted global recovery <sup>(a)</sup> (\$ million)**

	2021-22	2022-23	2023-24	2024-25
	Estimate	estimate	estimate	estimate
Income from transactions	(358.4)	(986.8)	(878.5)	(855.6)
Expenses from transactions	(183.0)	(514.0)	(528.3)	(525.7)
<b>Net result from transactions</b>	<b>(175.3)</b>	<b>(472.8)</b>	<b>(350.2)</b>	<b>(329.9)</b>
Other economic flows	(6.5)	(14.0)	(6.6)	(6.2)
<b>Net result</b>	<b>(181.8)</b>	<b>(486.8)</b>	<b>(356.8)</b>	<b>(336.1)</b>
<b>Net debt (cumulative)</b>	<b>181.8</b>	<b>669.7</b>	<b>1027.5</b>	<b>1364.7</b>
<b>Net debt to GSP ratio (percentage point difference)</b>	<b>0.04</b>	<b>0.13</b>	<b>0.19</b>	<b>0.23</b>

Source: Department of Treasury and Finance

Note:

(a) Figures may not add due to rounding.

## SENSITIVITY TO INDEPENDENT VARIATIONS IN MAJOR ECONOMIC PARAMETERS

Table A.3 presents the sensitivity of financial aggregates where the levels of key economic parameters identified in the table are 1 per cent (or, for interest rates, 1 percentage point) above the forecast for each year of the budget and forward estimates, holding all else constant.

The impacts shown are broadly symmetrical; that is, the estimated fiscal impacts would apply about equally in the opposite direction where there is a decrease in the parameter.

Differences in magnitude between positive and negative deviations in parameters may arise, though, in relation to income tax equivalent income because that line item is subject to a floor of zero; the impact on dividends may be affected by some entities facing caps on the share of profits that can be returned to the general government sector.

**Table A.3: Sensitivity of key fiscal aggregates to selected indicators being 1 per cent higher than expected from 2021-22 (\$ million)** <sup>(a)(b)(c)(d)(e)</sup>

	2021-22 <i>estimate</i>	2022-23 <i>estimate</i>	2023-24 <i>estimate</i>	2024-25 <i>estimate</i>
<b>GSP</b>				
Income from transactions	119	130	132	136
Expenses from transactions	3	(0)	(4)	(8)
<b>Net result from transactions</b>	116	131	136	144
<b>Net debt</b>	(116)	(247)	(383)	(527)
<b>Employment <sup>(f)</sup></b>				
Income from transactions	90	100	110	115
Expenses from transactions	320	334	350	364
<b>Net result from transactions</b>	(230)	(233)	(239)	(249)
<b>Net debt</b>	230	463	702	951
<b>Consumer prices <sup>(g)</sup></b>				
Income from transactions	285	305	310	323
Expenses from transactions	260	240	236	237
<b>Net result from transactions</b>	25	65	74	87
<b>Net debt</b>	(26)	(91)	(166)	(254)
<b>Average weekly earnings <sup>(h)</sup></b>				
Income from transactions	93	103	114	119
Expenses from transactions	4	2	(1)	(4)
<b>Net result from transactions</b>	89	101	114	123
<b>Net debt</b>	(89)	(190)	(305)	(427)
<b>Total employee expenses</b>				
Income from transactions	..	32	117	128
Expenses from transactions	321	336	353	368
<b>Net result from transactions</b>	(321)	(304)	(236)	(240)
<b>Net debt</b>	321	625	861	1101

	2021-22	2022-23	2023-24	2024-25
	estimate	estimate	estimate	estimate
<b>Domestic share prices</b>				
Income from transactions	..	..	..	..
Expenses from transactions	..	..	..	..
<b>Net result from transactions</b>	..	..	..	..
<b>Net debt</b>	..	..	..	..
<b>Overseas share prices</b>				
Income from transactions	..	..	..	..
Expenses from transactions	..	..	..	..
<b>Net result from transactions</b>	..	..	..	..
<b>Net debt</b>	..	..	..	..
<b>Property prices</b>				
Income from transactions	138	152	161	171
Expenses from transactions	(2)	(5)	(9)	(15)
<b>Net result from transactions</b>	140	156	171	186
<b>Net debt</b>	(145)	(306)	(479)	(668)
<b>Property transaction volumes</b>				
Income from transactions	64	70	74	77
Expenses from transactions	(1)	(2)	(4)	(7)
<b>Net result from transactions</b>	65	73	79	84
<b>Net debt</b>	(65)	(138)	(216)	(300)
<b>Interest rates <sup>(i)</sup></b>				
Income from transactions	118	113	110	107
Expenses from transactions	752	1266	1487	1725
<b>Net result from transactions</b>	(634)	(1153)	(1377)	(1618)
<b>Net debt</b>	<b>634</b>	<b>1523</b>	<b>2647</b>	<b>4027</b>

Source: Department of Treasury and Finance

Notes:

- Variations are applied to the economic variables effective from the first day in the budget year (1 July 2021). It is assumed that each variable's growth rate matches that under a no-variation scenario for the forward estimates period. This implies that the level of all economic variables (other than interest rates) is 1 per cent higher in level terms in each year of the budget and forward estimates. Interest rates are assumed to be 1 percentage point higher in each year of the budget and forward estimates.
- A positive number for income from transactions denotes an increase in revenue. A positive number for expenses from transactions denotes an increase in expenses (and hence a reduction in the net result from transactions). A positive number for the net result from transactions denotes a higher surplus or smaller deficit. A positive number for net debt denotes a higher level of net debt in the relevant year compared with a no-variation scenario.
- Only reasonably quantifiable impacts have been included in the analysis.
- Estimates of net debt are about equal to the cumulative impact of the net result from transactions. The difference between the cumulative net result from transactions and net debt is due to non-cash expenses and gross sale proceeds (where applicable).
- Figures may not add due to rounding.
- A shock to employment is assumed to impact payroll tax revenue to an extent consistent with no change to historical relationships between total employment, part-time/full-time employment shares and payroll tax revenue. Both public and private sector employment levels are assumed to be 1 per cent higher across the four years; the rise in public sector employment boosts general government sector employee expenses.
- Incorporates the impact of departmental funding model arrangements. It is assumed an increase in consumer prices in the budget year does not affect employee entitlements.
- A positive shock to average weekly earnings increases the expenses of public financial and non-financial corporations and reduces the general government sector's income from dividends and income tax equivalents.
- Interest rates are assumed to be 1 percentage point higher in each year of the budget and forward estimates.



## STYLE CONVENTIONS

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Figures in the tables and in the text have been rounded. Discrepancies in tables between totals and sums of components reflect rounding. Percentage changes in all tables are based on the underlying unrounded amounts.

The notation used in the tables and charts is as follows:

n.a. or na	not available or not applicable
1 billion	1 000 million
1 basis point	0.01 per cent
..	zero, or rounded to zero
tbc	to be confirmed
ongoing	continuing output, program, project etc.
(x xxx.x)	negative amount
x xxx.0	rounded amount

Please refer to the **Treasury and Finance glossary for budget and financial reports** at [dtf.vic.gov.au](http://dtf.vic.gov.au) for additional terms and references.





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**Victorian Budget 2021/22**

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