more than money

nab

FEDERAL Budget 2017

What the Federal Budget means for Small Business.

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ABOUT SMALL BUSINESS

We understand that small business is the backbone of our economy and our communities.

We take the time to listen and understand the challenges and opportunities your business faces. We know that you need the everyday to work seamlessly. And that in the moments that matter, we are there supporting you.

Helping you build a sustainable small business is our fundamental goal. When you succeed, we all succeed.

We recognise that knowledge is power, so we will make available to you insights based on our experience and quality analysis that comes with being Australia's number one bank for business.

And if you have not-so-small ambitions for your business, we're committed to helping you flourish with those too.

FEDERAL BUDGET OVERVIEW

Our Group Economics view

Alan Oster, Group Chief Economist, NAB

As expected, the centerpiece of this Budget is increased infrastructure spending, a new Housing Affordability plan, Gonski 2.0 and increased emphasis on the Operating Fiscal Balance ('good' versus 'bad' deficits). What was not expected was the new tax on banks liabilities – and at $6bn over the next four years it is not small. It is too early to say how banks will react.

On infrastructure, key elements include: the second Sydney Airport; the Melbourne to Brisbane rail freight line; Snowy Mountain funding; regional growth connectedness initiatives; and extra spending on hospitals. The package is valued at around $75bn over the next 10 years. For smaller business (up to turnover of $10m pa) the $20k instant write-off has been extended.

The Housing Affordability Package includes on the supply side: release of more Government land; tax incentives for private investment in affordable housing; establishing a new Government body to provide cheaper finance for community housing; a levy of $5k pa on vacant foreign owned housing; and seniors are allowed to transfer $300k into super from the sale of family homes to encourage downsizing. First home owners (FHOs) are now allowed to access voluntary contributions to super ($15k pa with a cap $30k) as a way of getting a deposit quicker. To the extent these measures are aimed at raising supply, they will clearly help – it is less obvious that boosting FHO's ability to build a deposit will do anything other than add to house price pressures.

Elsewhere, the Government has given up on 'zombie' measures of over $13bn currently stalled in the Senate. New initiatives in this space include Gonski 2.0 (an extra $18.6bn in school funding over the next decade) on a needs-based model; a university fee hike of 7.5%; higher repayments on government education loans; and a 2.5% efficiency dividend on universities.

The Health package includes the phased unfreezing of Medicare rebates for doctor visits and reduced costs for medicines. NDIS is now fully funded via a Medicare levy increase of 0.5% to 2.5% in mid-2019.

There is now going to be a one-stop shop for bank complaints and registration of senior bank executives and possible deregistration together with large fines for bad behaviour.

The government is emphasising the Net Operating Balance – effectively the Underlying Cash Balance less net investment on the government's balance sheet – which returns to surplus a year earlier in 2019-20. We have no objection to separating government debt into 'business as usual' spending from 'productivity enhancing investments'.

The key of course is whether the investment really is 'productivity enhancing'. That said, all debt has to be repaid. We (and the rating agencies) will continue to focus on the Underlying Cash Balance. In the 'Medium Term Economic Outlook', our view is that the Budget implies a further slight drag on growth near-term but a sharp drag thereafter.

We are much more cautious on 2018-19 forecasts and beyond. The economy in our view will be running nearer 2.5% than 3%+ by then. And we are very sceptical about the wages forecasts – and hence nominal GDP estimates. As such, we don't believe the medium term fiscal projections – and hence the credibility of the fiscal profile. This Budget will be popular, but from an economic perspective, if it looks too good to be true, it probably is.

Fiscal outcome

The underlying cash deficit is expected to fall from $37.6bn to $29.4bn in 2017-18, then rapidly improves to $2.5bn in 2019-20 – and achieves a surplus of $7.4bn in 2020-21. The Net Operating Balance, is however, expected to fall more aggressively (as extra government investment kicks in) to around $10.8bn in 2018-19 and achieves balance a year earlier in 2019-20.

Economic outlook

There is little fundamental difference between Treasury's and NAB's economic forecasts in 2017-18 – both around 3%. From a slow start in H1 2017 the economy will accelerate as lagged effects of higher commodity prices flow through to profits, LNG export volumes accelerate and the construction (apartment) cycle peaks. That said, domestic demand remains subdued. NAB's forecasts are notably more pessimistic as we move into the forward projections (from 2018-19) as near term positives start to unwind and the construction cycle turns down. Our expectations for the unemployment rate are similar, stabilising around 5.75% in the near-term before edging lower to 5.5% in the out years. We forecast nominal GDP growth of 3.3% in 2018-19 (the Government has 4%). The Government's nominal GDP numbers then accelerate further – heightening our skepticism. The Government's wages growth forecasts in particular, of 3% in 2018-19 and up to 3.75% by 2020-21, appear very optimistic.

Financial markets

There was little discernible market reaction to the Budget. That said, banks suffered as news of the new tax leaked out earlier in the day. Ratings agencies will clearly be looking at the underlying cash balance projections and their sustainability. It is equally unclear how they will see the new bank tax and what it means for growth and risk.

KEY INITIATIVES – SMALL BUSINESS

Small business groups' agenda for reform

Each year business organisations set out a wish-list of reforms as part of their pre-budget submissions. This year the list of recommended reforms included:

- Prolonging the life of the $20,000 asset immediate write-off introduced in the 2015 budget and scheduled to lapse in mid-2017. Some groups wanted a two-year extension to the measure, others wanted it made permanent and one wanted it kept and backdated to include small business assets bought before 2015.
- Increasing the size of the asset immediate write-off from $20,000 to $50,000, especially for farming and manufacturing.
- Giving all businesses with under $10m turnover access to the full range of small business tax concessions. The existing $2m threshold limits access to the capital gains tax concessions, as does the $5m threshold for accessing the tax discount for unincorporated small businesses.
- Cutting red tape, with NSW business surveys reporting half of firms saying regulatory burden has increased recently with state taxes like payroll a particular administrative concern.
- Combatting the delays in payment that harm cash flow in small business, with government urged to lead the way in prompt payment. The Australian Small Business Ombudsman has recommended legislation ensuring large businesses publicly disclose their payment times and practices, as well as new laws that set a maximum payment time.
- Introducing a new and simpler legal entity for small businesses in general and start-ups in particular. This should allow limited liability, income streaming and the retention of income in the new legal entity.
- Increasing funding for Export Market Development grants and no cutbacks in tax support for research and development activity.
- Introducing an investment allowance to support small business capital spending similar to that existing in 2008/9.
- Providing extra tax concessions for start-ups in their early years and business assistance programmes; and encouraging the provision of low cost seed capital for innovators.
- Supporting under-funded vocational education by funding traineeships, strengthening the apprenticeship system and emphasising career opportunities that vocational education can deliver through providing the skills that business needs.
- Government looking into the pros and cons of a new small business industry award, with the aim of lowering administrative costs.

What the budget actually delivers

The budget delivers some of the changes advocated by business groups:

- The $20,000 asset immediate write-off is to be extended for another 12 months and will now end in June 2018, after which Treasury says the threshold for immediate deductibility will revert to $1,000. This extension will cost around $950m in foregone revenue in 2018/19 and covers only small businesses with a turnover of under $10m spending on assets that are installed and ready for use by the end of June 2018.
- A National Partnership on Regulatory Reform will allocate $300m over two years from 2017/18 to States and Territories that remove unnecessary regulatory barriers and restrictions on competition, with a particular focus on regulatory reform that benefits small business.
- A levy on employers hiring foreign workers on certain skilled visas will finance a new Skilling Australians Fund. Around $1.5bn will be spent over four years from 2017/18 in training that prioritises apprenticeships and traineeships for occupations in high demand, growth sectors, occupations with high reliance on skilled migrants and to focus on training in regional and rural areas. The program should support 300,000 people in training over four years.
- A specialised industry mentoring system for Australian apprentices is to receive $60m in funding over two years from 2017/18 – it should support 45,000 Australian apprentices and trainees, especially in the first two years of their courses.
- The Government has tightened access to the small business capital gains tax concessions rather than extend their coverage as several business groups proposed. The aim is to ensure that the concessions can only be accessed by genuine small business owners and prevent the owners of larger operations from arranging their affairs to benefit from the concessions.
- Funding of an ACCC inquiry into retail electricity prices to assess whether power retailers' margins and profitability are in line with their costs and consider any impediments to consumer choice in power supply.
- Funding for ASIC that allows it to implement an extension of the Government's crowd sourced equity funding regime to include proprietary companies.

INDUSTRY REACTION

"A fresh start to fuel future growth." Australian Industry Group

The Australian Industry Group (AIG) thinks the budget "provides a substantial boost for smaller business by lowering tax burdens, extending asset write off eligibility and cutting red tape. It gives a welcome support for apprenticeships and traineeships through the new Skilling Australia Fund".

"The budget has potential to act as a catalyst for improved business confidence." Australian Chamber of Commerce and Industry (ACCI)

The ACCI says small business will be pleased to see the successful $20,000 asset immediate write-off continued for another year and made available to firms with turnover up to $10m. It also welcomed the new National Partnership on Regulatory Reform designed to cut State red tape, the new Skilling Australians Fund and the Federal Government's commitment to continue pursuing its agenda of cutting business taxes. The ACCI was less pleased by the increases in costs that employers will pay as levies when they bring in skilled foreign workers and which go to fund the Skilling Australians Fund.

"For the third year in a row, the Federal Government has demonstrated a genuine commitment to small business." Council of Small Business Australia (COSBOA)

COSBOA welcome the continuation of the $20,000 asset immediate write off and the availability of it and tax cuts to businesses with turnover up to $10m. It hopes the State Governments will show a pro-small business approach in the new National Partnership on Regulatory Reform and thinks that its focus should be on abolishing or reducing payroll taxes.

The Australian Small Business Ombudsman "welcomes the Government's small business Budget focus."

Besides welcoming continuation of the $20,000 asset immediate write-off (but being disappointed that it was not lifted to $50,000 as it proposed), the Small Business Ombudsman was disappointed by the lack of action on business payment times and conditions. It had wanted to see a National Payment Transparency Register to independently monitor payment terms and practices and the Government adopt a 15-day payments time to set an example that could greatly benefit small business cash flow if it were widely adopted by large businesses.

NAB'S VIEW

Although it has only been able to get tax cuts for businesses with turnover up to $50m through the Senate so far, the Government remains committed to the comprehensive business tax cuts outlined in last year's budget.

This tax cutting agenda implies considerable revenue losses – its 10-year cost was put at over $48bn by the Treasury Secretary last year and the annual cost of the company tax cut is estimated at $1.8bn in 2019/20, plus another $800m for the unincorporated small business tax discount.

Nevertheless, the Government's priority is on Australia's competitive position, given the falling trend in global business tax rates which President Trump's proposed steep US company tax cuts could aggravate.

While business should be pleased with the progress that has been made in lowering taxes and increasing the number of businesses eligible for concessional taxes, there is still plenty of unfinished business to fill out an ongoing reform agenda.

The multiplicity of turnover thresholds governing just who can access certain small business tax concessions looks set to remain a source of complexity and contention. Several business groups wanted to widen access to the capital gains tax discounts and the unincorporated small business tax discount in the latest budget but the Government failed to budge. We can expect the issue to return next year.

The absence of any mention of payments times and practices disappointed some business leaders, but the Budget may not be the best place to consider how to respond to the Small Business Ombudsman's report on existing payments arrangements.

After several difficult years, small business activity began to pick up a couple of years ago. Employment started growing again in small businesses, the entry rate of the smallest new businesses has picked up and exceeds their exit rate, ensuring that the stock of small businesses is again growing.

BUSINESS COMMENT

"Small business is at the centre of Australia's economic success. As Australia's largest business bank, we back business in the moments that matter. When small business succeeds, we all succeed.

Measures like major investment in infrastructure, instant asset tax write-offs, and incentives to cut red tape will help drive growth for small business in metro, regional and rural areas. We look forward to working closely with our small business customers over coming months."

Leigh O'Neill
Executive General Manager, Business Direct and Small Business

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