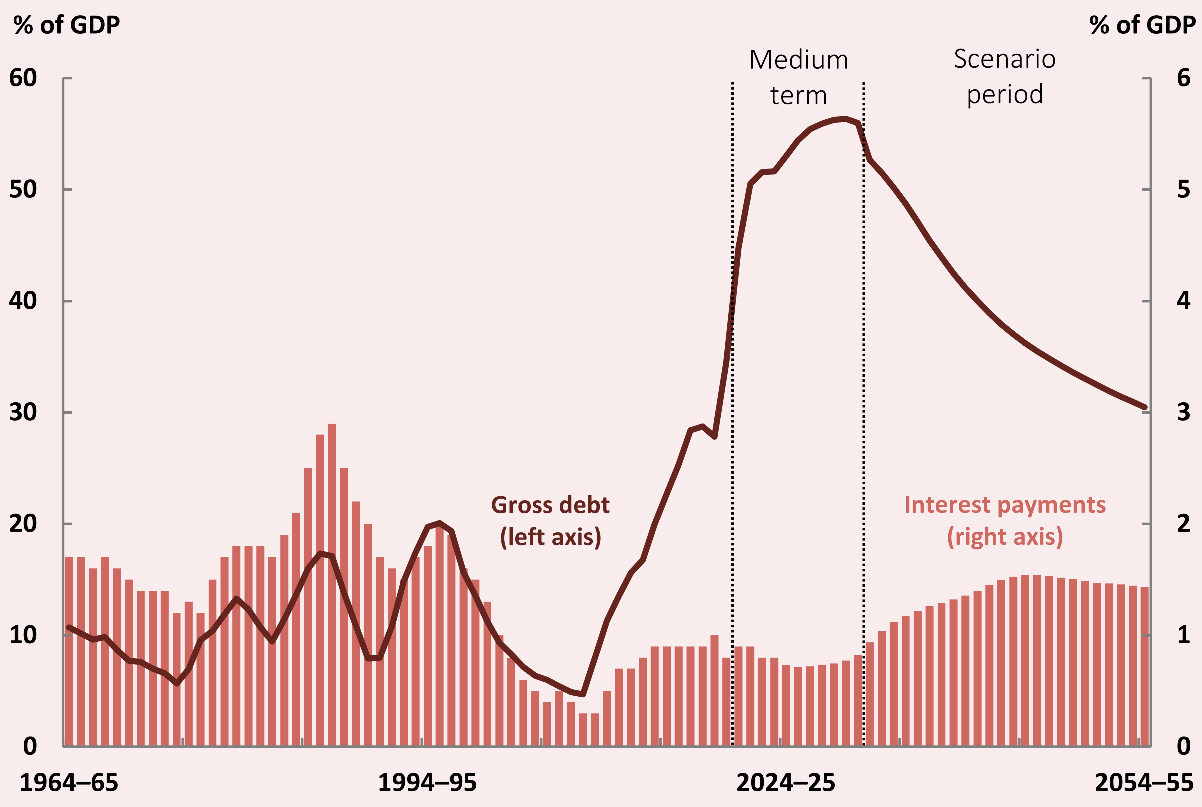
FISCAL SUSTAINABILITY

Assessing the long-term budget outlook

Parliamentary Budget Office

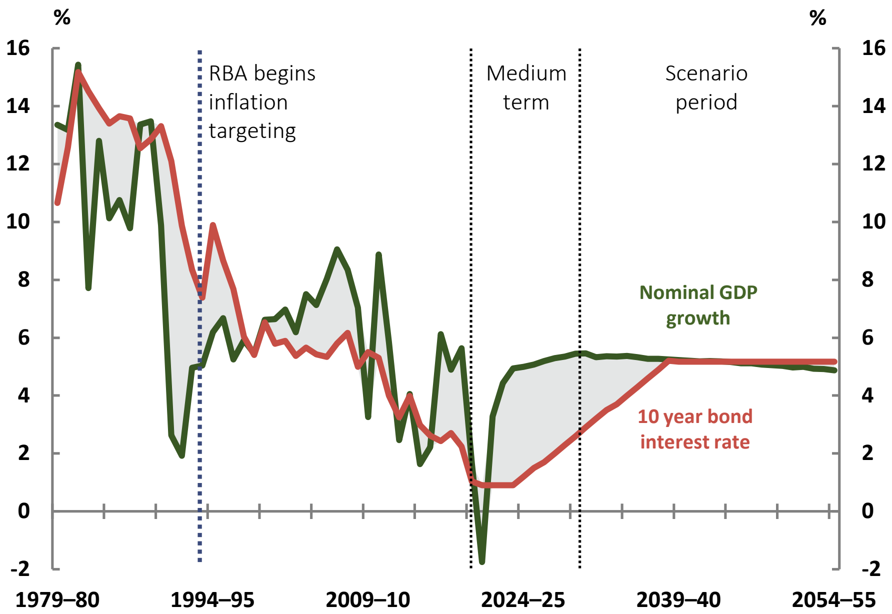
- The COVID-19 pandemic and the associated policy response will result in the largest Commonwealth Government debt since the Second World War, over 50 per cent of GDP.
- We have modelled scenarios for future debt for the 25 years after 2030-31 to assess if the fiscal position is sustainable.
- The path for future debt will depend on the three factors of: GDP growth; interest rates; and the budget balance.
- Our scenarios, with 27 different combinations of these three factors, show that the fiscal position is sustainable, with debt reducing in time, although this will require governments to continue to increase revenue and/or contain spending to return the budget balance to the average levels recorded over time. We don't know which scenario is most likely, but our 'best case' and 'worst case' are each very unlikely.
- Under our 'middle' scenario, debt steadily falls after 2030-31. Our 'best case' scenario (low interest rates, high GDP growth and small budget surpluses) results in the debt being largely eliminated. Our 'worst case' scenario (high interest rates, low GDP growth and a higher-than-average budget deficit) results in debt falling before slightly increasing later.
- The full report is available in the [Research reports] section of the PBO website.

FIGURE 1: Our middle scenario results in a steady decline in the debt-to-GDP ratio



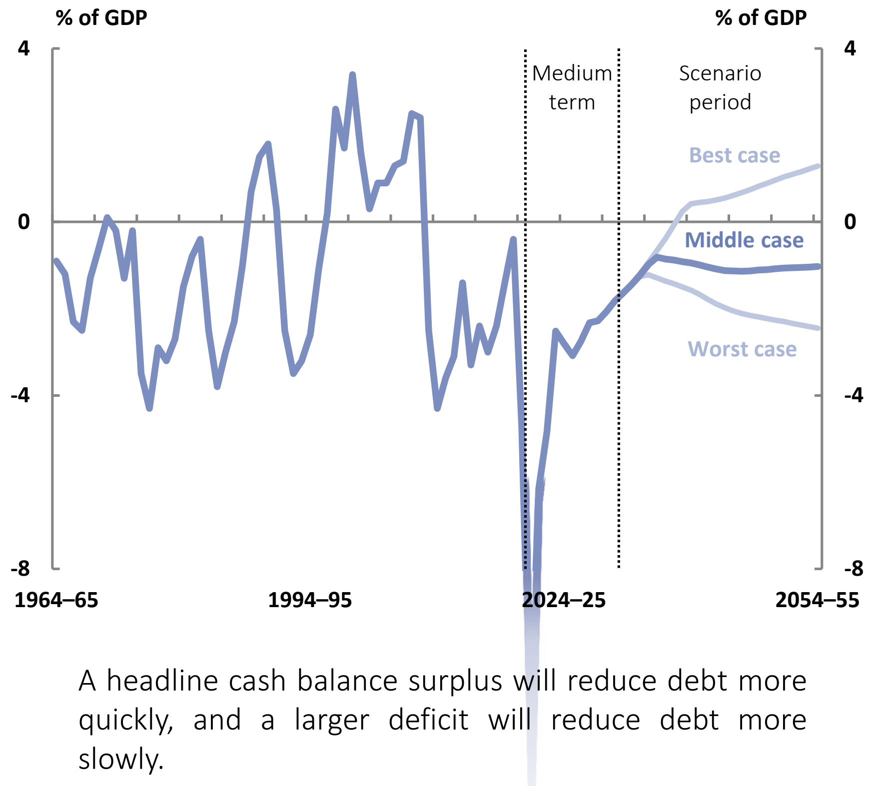
The scenario shows the path for debt as a share of GDP assuming the GDP growth and interest rates shown in Figure 2 (consistent with the 2020-21 Budget), and the budget balance shown to Figure 3: a modest deficit consistent with historical trends.

FIGURE 2: The path for debt depends on the difference between GDP growth and interest rates



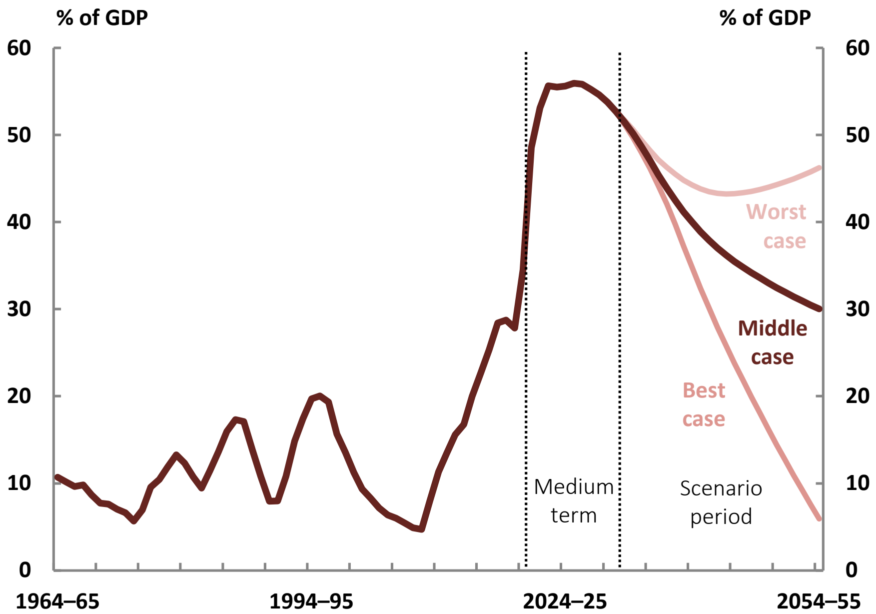
Interest rates are historically low, and expected to remain below nominal GDP growth for many years.

FIGURE 3: Our middle scenario assumes budget deficits broadly in line with historical averages



A headline cash balance surplus will reduce debt more quickly, and a larger deficit will reduce debt more slowly.

FIGURE 4: Our best and worst case scenarios for the debt-to-GDP ratio



The best and worst case paths show the bounds of our scenarios for the future path for debt, but they are each highly unlikely.