Federal Budget 2017

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EVANS & PARTNERS

The Research team reviews the implications of the 2017 Federal Budget

MACRO

The budget contains no material change in the governments' fiscal stance. Fiscal policy remains moderately contractionary. The government has used the windfall from higher commodity prices to fund its spending increases in education in particular. Overall, however, there is nothing here to scare currency and bond markets or ratings agencies so overall market responses will be minimal.

BANKS

The levy on liabilities will hit the banks bottom line by a combined $1.5 billion per year and there will be also be another rise in compliance costs from greater oversight measures. Implications for MQG unclear at this stage.

CONSUMER AND MEDIA

A small positive from the tax cut to high income earners that will be worth 0.1-0.3% of retail spending depending on how much is saved. Rule changes in media are generally positive.

HEALTHCARE

Measures were largely as anticipated on incentive fees for pathology and imaging, changes to indexation of bulk billing incentives and changers to the Pharmaceutical Benefits Scheme.

DEVELOPERS

Most of the measures are relative small. However the limits on foreigners buying more than 50% of large developments might affect MGR.

INFRASTRUCTURE

Most of the projects have already been well communicated

Macro

The budget contains no material change in the governments' fiscal stance. Fiscal policy remains moderately contractionary, and there is now a more rapid improvement in the fiscal balance by 2021.

Economic forecasts are generally conservative in the short term on growth and commodity prices – unlike in previous years. However they are a little aggressive from 2019 onwards at 3%. The consensus of forecasters would be closer to 2.5% to 2.75%. This more-rapid growth helps the government show a surplus in 2020-21.

The Budget should probably have been better this given the surge in commodity prices but it has been this windfall that has been used to fund higher spending. Spending is forecast to rise by 4.2% per year, a noted acceleration from the past two years.

Overall, however, there is nothing here to scare currency and bond markets or ratings agencies so overall market responses will be minimal apart from some of the sector implications discussed below.

Banks

Liabilities Levy – this will hit the bottom line

a. 6bps levy on banks liabilities for banks with liabilities over $100b (ie major banks & Macquarie)

b. Starts 1 July 2017

c. Customer deposits <$250k and additional capital requirements will not be levied

We expect the banks come out shortly with some detail on the impact, as current disclosures around deposits amounts are not readily available.

For an estimation:

- we subtract deposits held in retail/consumer segments, which are typically low in value.
- In doing this get pretty close to Treasuries stated amount of ~$1.5b in the first year. We will look for further clarity from the banks on specific amounts and impacts.
- Impact on earnings ranges from 4-6% across the majors.
- We would expect more weakness tomorrow based earnings impact, but today's selloff will have captured much of this
- The impact on MQG will depend on whether the levy applies to the Bank or the entire group. This will need to be clarified.

Bank	Liabilities	Less Retail Deposits	Levied Liabilities	Annual Levy ($m)	FY18e NPAT	Earnings Impact
ANZ	838,600	106,811	731,789	439	7,665	-6%
CBA	909,907	219,762	690,145	414	10,278	-4%
NAB	739,971	112,900	627,071	376	7,269	-5%
WBC	780,621	185,900	594,721	357	8,747	-4%
			Total	1,586		

Conduct/Oversight measures – may increase compliance cost but not materially

a. Bank Executive Accountability regime

b. Senior executives must register with APRA

c. Heightened accountability with new mandatory reporting requirements

d. Fines starting at $50m for small banks and $200m for large banks

e. A permanent team will be established by the ACCC to investigate competition

f. Measures to make data sharing between banks

Consumer

Key changes:

- The expiring 2% budget repair levy on individuals paying more than $180,000 has not been extended. However, the Medicare levy does increase for all in 2019.
- The accelerated depreciation allowance of $20,000 for small businesses has been maintained. The incremental benefit to retailers will be small.

Implications:

The tax cut for high income earners is worth about $1 billion (or 0.3% of total retail sales). However those on high incomes will not spend all of that. There are no major listed stocks with a significant exposure to spending by high income earners.

Media

Key changes:

- Gambling ads banned during live sports broadcasts before 8.30pm, and for five minutes before and after start of play
- $130 million annual licence fee for FTA TV broadcasters will be scrapped in favour of a $40 million spectrum fee
- Repealing the 75 per cent reach rule and 2 out of 3 cross-media ownership laws

Implications:

Overall, if the media reforms are passed, we believe it will:

1. Improve profitability of FTA TV broadcasters and increase their ability to invest into content

2. Enable greater consolidation between media assets. This could deliver larger scale to reach greater audiences and also allow extraction of cost synergies. It could also potentially enable exit and crystallisation of value of structurally challenged assets.

Developers - SGP, MGR

Expect modest positive impact from the First Home Super Saver Scheme given the benefits (effectively the tax concession on a maximum $30k contribution) is not as significant for the average individual/couple ($10-15k benefit for the average couple over 2-3 years). A similar measure was introduced in 2008 with no success. The key issue remains the lack of affordable product / land supply in our view. Expect SGP to benefit the most out of the developers given its larger exposure to FHBs.

Commitment to identify under-utilised commonwealth land for residential development. The Government will publish a registry of land holdings online to create the opportunity for stakeholders to propose better use of land. This process is positive for developers as it could accelerate land release - a key issue particularly in Sydney.

Measures on Foreign Buyers - potential impact on MGR given high-density exposure. No impact on SGP.

- Foreign buying in new developments capped at 50%. Major listed developers already have caps at ~30% of lots/apartments. 2nd/3rd tier developers could be more impacted given the over reliance on FIRB buyers. This measure could help apartment construction moderate to more sustainable levels.
- Changes in CGT for foreign investors. The removal of Main Residence CGT exception, the increase in the foreign resident capital tax withholding rate from 10% to 12.5% and the lowering of the CGT withholding threshold from $2m to $0.75m are likely to have a modest negative impact on demand (limited impact on demand from VIC's increase in foreign property tax last year).
- Charge on foreign-owned vacant houses. In our view this would minimal impact on FIRB demand.

Infrastructure - SYD, TCL

Most of the spend going to the Western Sydney Airport ($5.3b) and rail projects (i.e. no impact on TCL). The Government's commitment to the WSA has been well communicated (with or without SYD's involvement). We remain of the view the Government could look extend the proposal to 3rd parties now that SYD has formally rejected the proposal.

Healthcare

Budget specifics were largely leaked to the press and therefore there were no real surprises. Expectations of an improved regulatory environment for collection centre rentals may be cause for some disappointment. However, we had not anticipated any changes to the collection centre cost base given the unlikely removal of bulk billing incentive payments in the first place. Importantly we note, there was no discussion on the affordability of Private Health Insurance nor any savings announced from the Prostheses list. Both these items remain a work in progress for the Government.

Pathology

Collection Centres

The Federal Budget confirmed an anticipated back flip on the scrapping of the Bulk Billing incentive fees in pathology and diagnostic imaging. This is clearly an attempt to re-establish itself as a Medicare Friendly Government. Similarly, the Government has not followed through with addressing the burgeoning collection centre rental costs for the industry. Under the original Pathology Australia agreement, the Government intended to scrap bulk billing incentive fees and in a quid pro quo for the industry, rein in collection centre rents. The 2017-18 Budget effectively proceeded with neither of these initiatives. In somewhat of a token gesture, $18m has been earmarked for the strengthening of the compliance of Collection Centres via audits and data analytics to ensure arrangements between doctors and collection centres are conducted in accordance with the existing provisions of the Health Insurance Act 1973. Previously, the Government had intended to introduce provisions to the Health Insurance Act to clarify the meaning of the term "market value" by linking it to relative local commercial market rents.

Implications

EAP comment

The absence of the clarification of the term "market rents" significantly reduces the ability for the pathology operators (SHL and PRY) to achieve material savings from collection centre rentals. Whilst it was no secret that the Government was unlikely to proceed with the scrapping of the Bulk Billing Incentive Payments there has been some market expectations that the Coalition would address collection centre rental arrangements regardless. **The absence of the clarification of "market value" is a net Negative to both SHL and PRY.**

MBS fee increase for cervical cancer

The Budget flagged a specific increase in the MBS fee for cervical cancer cytology tests from 1 May 2017. The MBS fee is set to increase from $19.45 per test to $28 per test.

EAP comment

This is favourable development for both SHL and PRY but is not material. Total cost to the Government is ~$25m for the initiative which would be split amongst several operators.

Medicare Benefits

Medicare Benefits Schedule

$1b will be provided across 4 years from 2017-2018 for the phased reintroduction of indexation for certain items on the MBS. Specifically;

- Bulk billing incentives for GPs will be indexed from 1 July 2017. Incentive fees are generally payable for bulk billing services to those below 16 years and pensioners
- Standard consultations by GPs and specialist attendances will be indexed from 1 July 2018

- Specialist procedures and allied health services will be indexed from 1 July 2019

Indexation will be introduced for certain diagnostic imaging items from 1 July 2020. These include computed tomography scans, mammography, fluoroscopy and interventional radiology

Continuation of MBS review

Government to continue work on the Medicare Benefits Schedule. **$44.2m to be committed across 3 years**

Development of the Health Care Home trial

Government to further develop the Trial of Health care homes. The trial is set to commence with 20 selected general practices from 1 October 2017 with the remaining 180 from 1 December 2017. **Timing of spend delayed** with 2017-2019 costs now expected to be incurred in 2019-2020.

EAP comment

The reintroduction of GP MBS indexation was in line with the markets expectation following recent media leaks. Beneficiaries would include PRY and to an extent SHL through its IPN business. PRY management alluded to a $5m benefit should the MBS be lifted. On our estimates that is ~5% to FY18 Reported NPAT. The deferral in expenditure by ~2 years for the trial of health care homes is noteworthy as it highlights the further work that is required before this initiative gathers meaningful momentum in redefining the delivery of primary care.

Vaccinations

National Immunisation Program awareness and expansion

Government is providing an additional ~$20m over 4 years to increase awareness and to offer free catch-up childhood vaccinations for children and young adults aged between 10 -19 years of age.

EAP comment

CSL is likely beneficiary to this program expansion but any benefit would be immaterial to the Group.

Influenza, antivenoms and Q-fever

The Government will provide funding to support the ongoing production of pandemic influenza vaccines, antivenoms and Q-fever vaccines. The cost associated with this program was not available for publication due to commercial in confidence considerations.

EAP comment

CSL is likely beneficiary to this funding support. However, we expect it will be immaterial to the CSL Group.

Aged care - No change to ACFI as expected.

Pharmaceutical Benefits Scheme

PBS new and amended listings

- $1.2b will be provided across 5 years from 2016-2017 for new and amended listings on the PBS.
- Specific drugs include Sacubitril with Valsartan for treatment of heart failure, Nintedanib for idiopathic pulmonary fibrosis and Paliperidone for schizophrenia.

PBS cheaper medicines

- $1.8b savings across 5 years from 2016-2017 to 2021-2022 expected from reducing prices of drugs that have been on the PBS based on tiers effectively larger cuts to drugs that have been on the PBS for longer.

EAP comment

Net cuts ($160m - $200m) YoY from the latest changes to the PBS. Potential negative for distributors in the listed space; SIG (Not covered) and API (Not covered)

Summary table of key budget reforms

Source: 2017/2018 Budget

Components	2017/2018	2018/2019	2019/2020	2020/2021
Pathology and Collection Centre	6.0	2.7	2.7	2.7
Pathology MBS freeze increase for cervical cancer	28.3	0.2	- 0.1	9.7
Pathology cuts (not proceeding)	215.8	225.2	234.6	
MBS indexation	9.5	146.0	403.4	443.3
Development of Health care Homes trial	- 22.1	- 2.5	25.6	-
Continuation of MBS review	15.9	15.7	12.7	-
Vaccinations National Immunisation Program awareness	0.6	6.8	5.3	5.3
Antivenon	NFP	NFP	NFP	NFP
PBS new drugs	213.3	264.1	312.3	346.2
PBS cheaper medicines	-24.7	-364.5	-427.1	-476
PBS price ammendments	-64.5	-65.4	-63.4	-61.8

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