

## 1.2 FISCAL STRATEGY – FINANCIAL OBJECTIVES AND KEY MEASURES

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### Fiscal Strategy

The Government remains committed to the principles of responsible financial management.

In the 2011-12 Budget, the Government will meet its plan of returning the Budget to surplus by 2013-14 alongside the delivery of services in priority areas, to meet the needs of Canberrans.

The Government continues to maintain its fiscal strategy, which has been successful in dealing with cushioning the effects of fiscal shocks experienced in preceding years.

The Government's financial objectives and key measures are:

- to achieve a General Government Sector Net Operating Surplus;
- to maintain operating cash surpluses;
- to maintain a AAA credit rating;
- to manage debt prudently and maintain net financial liabilities within the range of all AAA rated jurisdictions;
- to fully fund the Territory's unfunded superannuation liability by 2030;
- to maintain quality services and infrastructure;
- to make targeted investments to achieve strategic objectives of economic growth, reducing future costs and addressing chronic disadvantage; and
- to maintain taxation revenues at sustainable levels.

With the assistance of savings measures incorporated in this and past Budgets, the underlying expenditure trajectory has been lowered, with compound annual average growth rate over the Budget and forward estimates period being reduced by around  $\frac{3}{4}$  per cent per annum.

Further information on the Budget Plan is provided in Budget Paper No. 3, Chapter 1.3 *The Budget Plan Update*.

## Objective: Achieve a General Government Sector Net Operating Surplus

The Government's objective is to achieve a net operating surplus: temporary deficits must only occur if they are offset by surpluses at other times.

The Government adopted a Budget Plan in the 2009-10 Budget to return to surplus by 2015-16. The Plan has been updated to take account of changes in the economy, revenue growth and new policy initiatives, and now targets achieving a surplus by 2013-14. This target will be achieved in this Budget.

The Net Operating Balance for the Budget and forward estimates has improved as a result of:

- strong housing market and land sales activity;
- higher dividends from the PTE sector;
- further savings measures incorporated to improve efficiency in the delivery of services  
offset by:
- substantial GST revenue reductions resulting from changes in relativities since the 2010-11 Budget Review and an estimated downward revision in the national GST Pool.

**Table 1.2.1**  
**The Budget Operating Surplus/Deficit**

	2010-11	2011-12	2012-13	2013-14	2014-15
	Est.Outcome	Budget	Estimate	Estimate	Estimate
	\$m	\$m	\$m	\$m	\$m
<b>UPF Net Operating Balance</b>	<b>11.7</b>	<b>-115.6</b>	<b>-112.8</b>	<b>-92.9</b>	<b>-43.4</b>
Plus: Expected Long-Term Capital Gains on superannuation Investments <sup>1</sup>	7.9	78.7	88.9	94.5	100.0
<b>Headline Net Operating Balance</b>	<b>19.7</b>	<b>-36.9</b>	<b>-23.9</b>	<b>1.6</b>	<b>56.6</b>

**Note:** Table may not add due to rounding.

1. This component of the Territory's overall returns from superannuation assets varies with assumed changes in the strategic allocation of assets held in the Superannuation Provision Account (SPA). However, in all years this adjustment, together with interest and dividend revenues, provides for expected returns on the total superannuation asset portfolio of 7.5 per cent per annum.

The primary measure of the Budget is the Headline Net Operating Balance adjusted for long-term expected capital gains on superannuation assets (consistent with a long-term expected rate-of-return of 7.5 per cent). This measure allows the ACT Budget to be compared on a "like for like" basis with the Net Operating Balances reported by other jurisdictions.

The ACT's superannuation investments are structured in a form that makes the ACT's net operating balance appear weaker relative to other jurisdictions. This difference arises because state governments generally hold their superannuation investments in forms that allow the expected capital gains on these investments to be implicitly included in the calculation of their GFS Net Operating Balance<sup>1</sup>.

1. State governments have typically injected assets into their public sector superannuation schemes to partly fund those schemes. Under Australian Accounting Standard 119, *Employee Benefits*, the expected rate of return on these assets can be subtracted in determining the total superannuation expense each year. Because the expected rate of return reduces the annual superannuation expense, it has a direct impact on the General Government Sector Net Operating Balance. This same treatment is used by state governments in preparing their GFS financial statements. A further discussion of this accounting treatment is provided in Victoria's 2004-05 Financial Report (at page 23). This report can be accessed at [www.dfvic.gov.au](http://www.dfvic.gov.au). This treatment is not applicable to the ACT, because, unlike state governments, the ACT is precluded from holding its superannuation assets in the CSS and PSS funds. The superannuation assets are instead held in the Superannuation Provision Account, a statutory fund in the General Government Sector.

This is a significant matter for the ACT as the long-term capital gains on superannuation investments range from \$78.7 million in 2011-12 to \$100 million in 2014-15.

To ensure that the ACT’s Budget is measured on a consistent basis with other jurisdictions, it is necessary to adjust the Net Operating Balance for expected capital gains on superannuation investments. This adjustment is not simply required to ensure consistency with the Net Operating Balance results reported by state jurisdictions, it is also required to provide an accurate assessment of the longer term sustainability of the budget position.

This is because the operating budget takes into account the accruing expenses on long-term superannuation liabilities. These superannuation expenses will be paid over the next forty to sixty years. The Government’s superannuation investments held in the Superannuation Provision Account (SPA) are intended to help fund these future cash payments. Long-term capital gains on investments (for example, increases in the value of investments held) provide a source of funding for the long-term superannuation liabilities. Consequently, it is necessary that these long-term average gains be taken into account when assessing the budget operating position.

**Objective: To Maintain a AAA Credit Rating**

The current ACT Government credit rating provided by Standard & Poor’s Rating Services is a ‘AAA’ (Triple A) long term credit rating and a ‘A-1+’ short term credit rating, in both local and foreign currencies.

The ‘AAA’ and ‘A-1+’ ratings are the highest ratings assigned by Standard & Poor’s. Standard & Poor’s assessed the outlook for the ACT’s finances as continuing to be ‘Stable’.

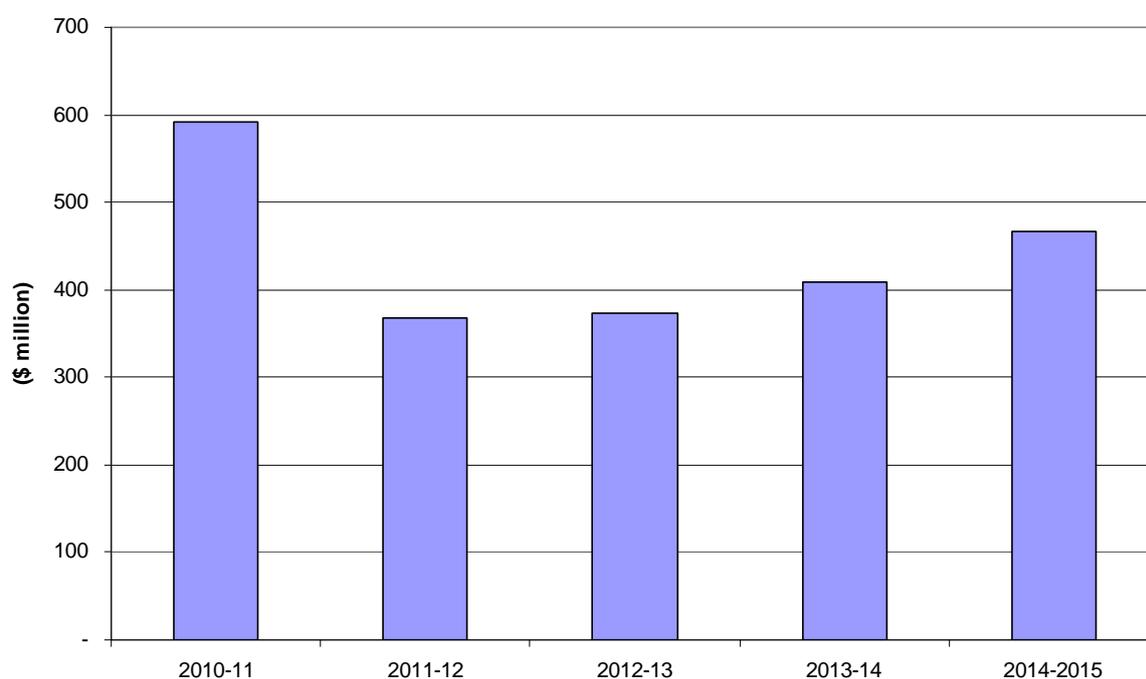
	Local Currency Long Term	Local Currency Short Term	Foreign Currency Long Term	Foreign Currency Short Term
Standard & Poor’s	AAA	A-1+	AAA	A-1+

## Objective: Maintain Operating Cash Surpluses

The Government's objective is to maintain operating cash surpluses in the General Government Sector at all times. The operating cash balance measures all operating cash receipts each year (for example, taxes, fees and fines, and operating grants from the Commonwealth Government) less all operating cash payments (including wages and salaries, cash superannuation payments and payments for goods and services).

Figure 1.2.1 below shows that the General Government Sector Operating Cash Surplus is expected to be \$372.3 million in 2011-12, with surplus balances across the forward estimates. A revised operating cash surplus of \$592.4 million is estimated for 2010-11. A strong operating cash balance ensures that there is sufficient cash generated from operations to cover the net outlay of the capital investment, to repay debt, and to put aside to address unfunded superannuation liabilities.

**Figure 1.2.1**  
**Net Cash Flows from Operating Activities: General Government Sector**



## Objective: Maintain a Strong Balance Sheet

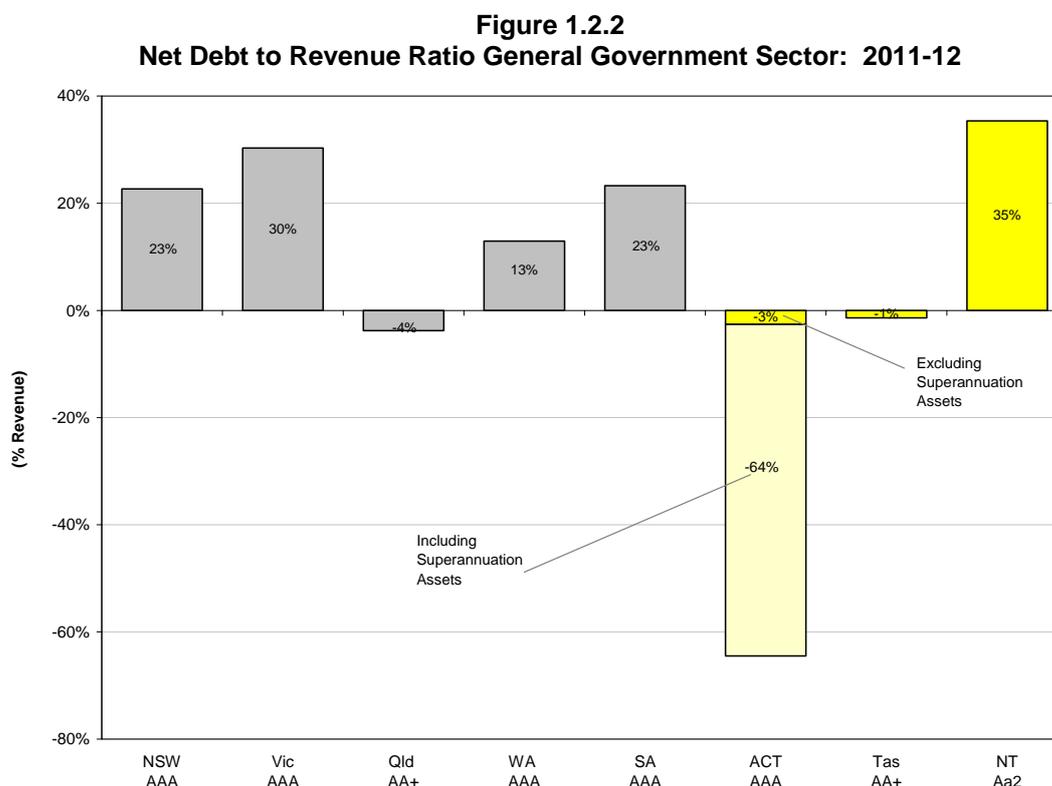
The ACT continues to have one of the strongest balance sheets of any Australian government. The measures announced in past budgets and continued in the 2011-12 Budget, combined with an overall improvement in the Australian economy will ensure the balance sheet remains strong. The ACT continues to maintain capacity to support high-priority investments, enabling it to provide high quality services expected by the ACT community. Below are the key measures of the General Government Sector's balance sheet.

### Net Debt

A key balance sheet measure in the GFS framework is the net debt to revenue ratio, which takes into account gross debt liabilities as well as financial assets (such as cash reserves and investments). The Commonwealth Government, for example, highlights net debt as the key measure of government debt.

Figure 1.2.2 below shows that the ACT is estimated to have negative General Government Sector net debt in 2011-12. This indicates that the Territory's General Government Sector cash reserves and investments are greater than its gross debt liabilities. As indicated, net debt for some States, including the ACT and Queensland, is reduced due to the impact of investments held to fund superannuation liabilities. However, if these assets are excluded, the ACT has negative net debt equivalent to around three per cent of revenue.

The figures below have been sourced from other jurisdictions' Mid Year Budget Review releases.



Source: The interjurisdictional data utilised in this comparison is taken from each jurisdiction's 2010-11 Budget Mid-Year Review.

## Net Financial Liabilities

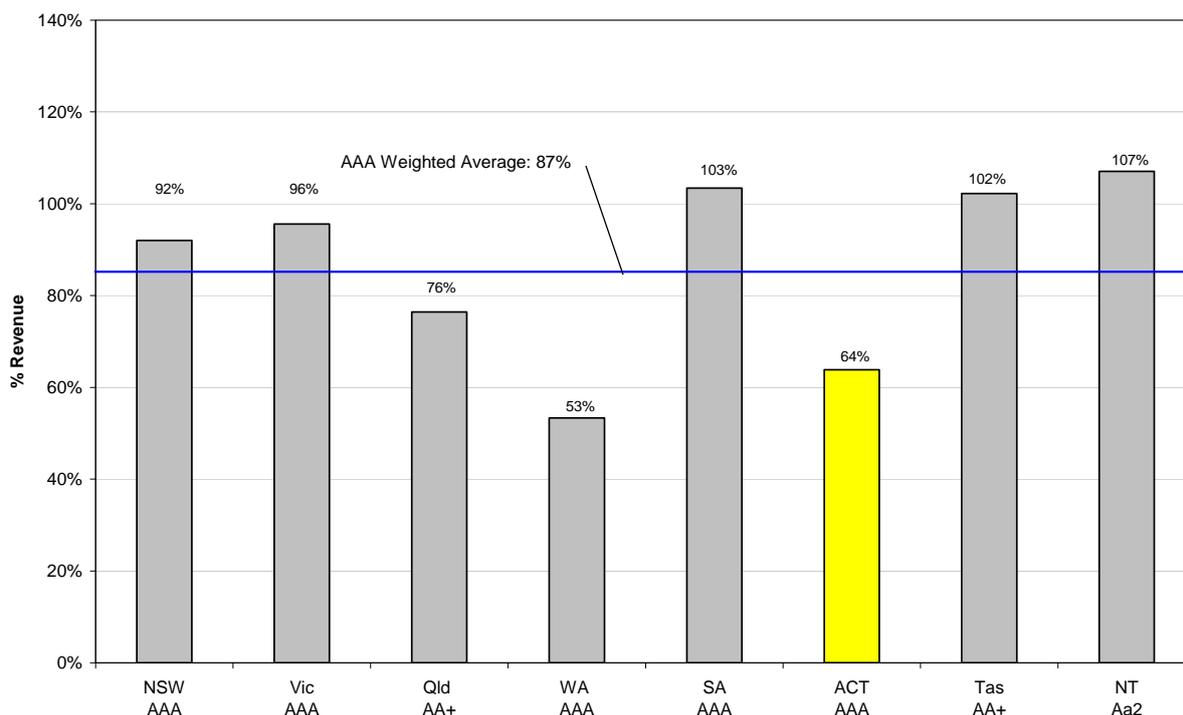
Net financial liabilities are a broad measure of General Government Sector liabilities, including net debt and superannuation liabilities. The net financial liability has increased to 64 per cent, compared to 62 per cent in the 2010-11 Budget. The ACT continues to have a strong balance sheet, and remains below the weighted average level for all AAA rated jurisdictions.

Net financial liabilities are calculated as total liabilities less financial assets (such as cash reserves and investments). It takes into account all non-equity financial assets, but excludes the value of equity held by the General Government Sector in public corporations (for example, ACTEW Corporation).

The ratios appearing in Figure 1.2.3 for all other jurisdictions are based on their Mid Year Budget Reviews.

Figure 1.2.3 below compares the ACT's net financial liabilities as a proportion of revenue with other jurisdictions. It shows that the ACT continues to have one of the lowest net financial liabilities, compared to other jurisdictions; and is below the weighted average level for all AAA rated jurisdictions.

**Figure 1.2.3**  
**Net Financial Liabilities to Revenue Ratio General Government Sector: 2011-12**



Source: The interjurisdictional data utilised in this comparison is taken from each jurisdiction's 2010-11 Budget Mid-Year Review.

A key question for governments is whether to borrow to invest in new capital assets. It is widely recognised as appropriate for governments with strong balance sheets to incur some debt, provided the debt is used to finance high quality assets in areas of community need. This is because these assets (for example, new roads, schools and hospital facilities) provide benefits to the community over a long period of time.

It is important, however, that the level of debt is sustainable. The ratio of net financial liabilities to revenue provides an indicator of the sustainability of a jurisdiction's debt.

The Government's objective is to maintain this ratio within the range of all AAA rated jurisdictions in Australia. While this ratio is subject to volatility (in particular, net financial liabilities can fluctuate, sometimes substantially, depending on the condition of financial markets), it is desirable that it remains broadly stable over time.

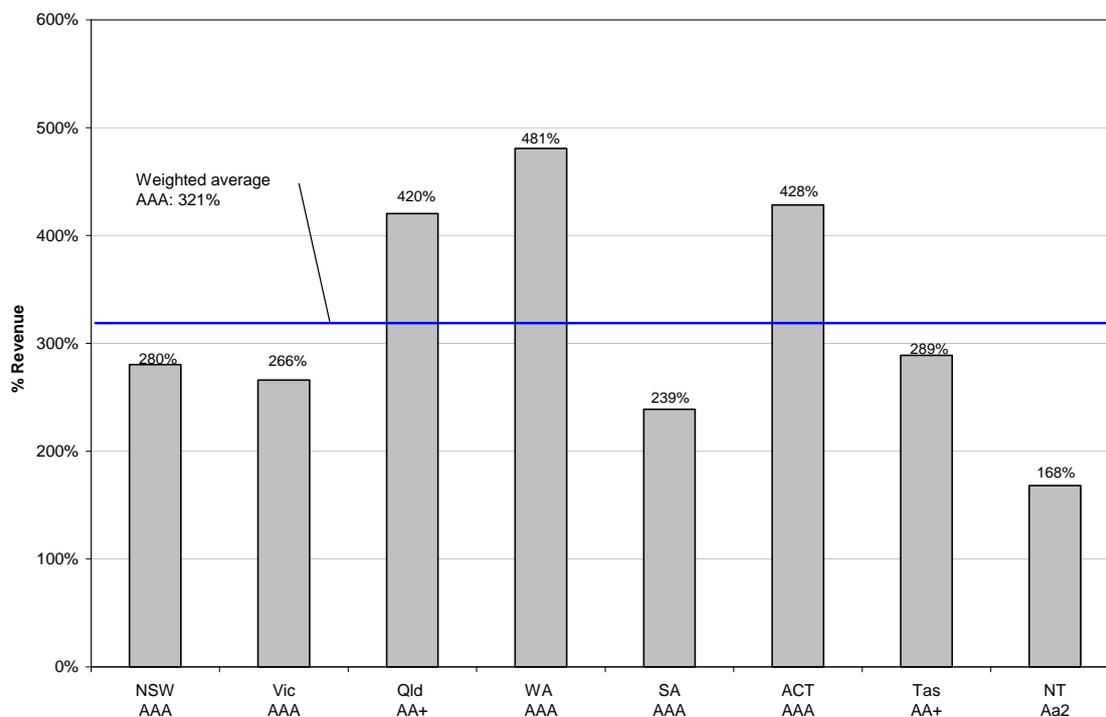
The 2011-12 Budget anticipates new general government sector borrowing for capital purposes of up to \$350 million in 2011-12 and an additional \$300 million in 2012-13. This is an increase of \$200 million on the level estimated in the 2010-11 Budget. The infrastructure investment funded by this debt will assist the ACT economy, consumer confidence, and most importantly, enhance service delivery for ACT residents.

Even with these borrowings, and the reductions in financial assets, the Territory's net financial liabilities to revenue ratio is estimated to be within reasonable levels across the Budget and forward estimates.

## Net Worth

The broadest measure of a jurisdiction's balance sheet is net worth, which measures the total value of all assets less all liabilities. The ACT has strong positive net worth, and as a proportion of revenue, one of the strongest of all Australian jurisdictions.

**Figure 1.2.4**  
**Net Worth to Revenue Ratio General Government Sector: 2011-12**



Source: The interjurisdictional data utilised in this comparison is taken from each jurisdiction's 2010-11 Budget Mid-Year Review.