

Australian Capital Territory Government Management Discussion and Analysis for the Financial Year Ended 30 June 2018

The 2017-18 Management Discussion and Analysis represents the consolidated Total Territory's financial results.

ACT Economy in 2017-18

The ACT economy is continuing to experience a period of sustained strong growth and is expected to be on track to meet the 2018-19 Budget estimate of 4½ per cent growth in Gross State Product in 2017-18, following 4.6 per cent growth recorded in 2016-17.

The ACT's State Final Demand grew by 4.4 per cent in 2017-18, in year average terms, which is slightly above the 2018-19 Budget estimate of 4.0 per cent growth for 2017-18. This robust outcome was broadly-based, with all major components of State Final Demand contributing positively to growth.

Employment grew by 2.2 per cent, equating to the creation of around 5,000 new jobs in 2017-18. The unemployment rate remained low at 3.7 per cent in June 2018.

The ACT's population grew by around 8,500 people over the year to March 2018 (up 2.1 per cent from March 2017).

The Economic Outlook

Looking forward, the expansion of the ACT economy is expected to continue, with a forecast of 3½ per cent growth in Gross State Product in 2018-19.

Administrative Changes

On 1 July 2017, the Land Development Agency was ceased and the Suburban Land Agency and City Renewal Authority were created.

From 1 October 2018, the Health Directorate separated into two distinct organisations with the Canberra Health Services responsible for ACT Health's clinical operations and the ACT Health Directorate responsible for strategic policy and planning.

Note: Forecasts and projections are rounded to a ¼ of a percentage point, reflecting an appropriate level of accuracy in forecasting economic parameters. Projections are based on long-run trend assumptions.

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The Uniform Presentation Framework (UPF) Operating Result for the Total Territory is a deficit of \$42 million, which is lower than the deficit of \$331 million as forecast in the 2017-18 Budget by \$289 million (87.3 per cent) and lower than the 2016-17 deficit of \$237 million by \$195 million (82.3 per cent).

Total revenue for 2017-18 of \$5,692 million was \$256 million (4.7 per cent) higher than the 2016-17 result of \$5,436 million. This was mainly due to an increase in Commonwealth grants.

Total expenses for 2017-18 of \$5,734 million was broadly in line with the 2016-17 outcome of \$5,673 million.

Net Financial Liabilities at 30 June 2018, were \$9,553 million which is \$856 million (9.8 per cent) higher than the 30 June 2017 result of \$8,697 million, predominantly due to a change in the estimation of the defined benefit superannuation liability.

The Total Territory's Net Debt (excluding superannuation investments) at 30 June 2018 of \$2,804 million was broadly in line with the 30 June 2017 result of \$2,781 million.

Future Trends

In 2018-19 and across the forward estimates, the Territory will continue its focus on mitigating financial risks by maintaining expenditure levels within budget in an environment where pressures on the net cost of service delivery are significant.

Across the forward estimates period, the Territory's UPF Operating Result is estimated to increase from a deficit of \$131 million in 2018-19 to a \$217 million deficit in 2021-22.

Net Debt (excluding superannuation investments) is expected to increase from \$3,744 million to \$4,630 million in 2021-22, driven largely by the expected inclusion of lease liabilities associated with the ACT Law Courts Facilities and Canberra Light Rail Stage 1 Public Private Partnership projects.

Net Financial Liabilities are estimated to peak at \$9,807 million in 2021-22 due to forecast growth in the superannuation liability and the inclusion of lease liabilities associated with the Public Private Partnership projects.

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Total Territory

Financial Performance

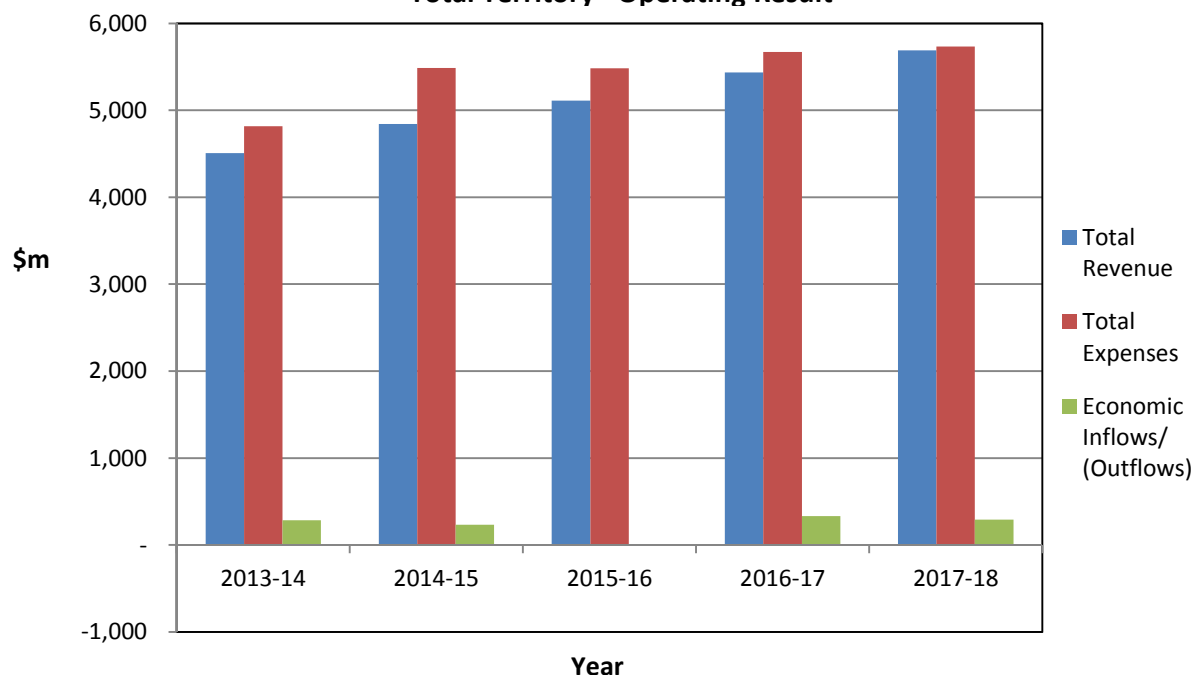
Table 1.1 shows the UPF Operating Result for the Total Territory is a deficit of \$42 million, which is lower than the deficit of \$331 million as forecast in the 2017-18 Budget by \$289 million (87.3 per cent) and lower than the 2016-17 deficit of \$237 million by \$195 million (82.3 per cent).

**Table 1.1
Total Territory - Operating Result**

	2016-17	2017-18	2017-18	2018-19	2019-20	2020-21	2021-22
	Actual	Actual	Annual Budget	Annual Budget	Forward Estimate	Forward Estimate	Forward Estimate
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Total Revenue	5,436	5,692	5,649	6,077	6,209	6,489	6,754
Total Expenses	5,673	5,734	5,980	6,209	6,397	6,746	6,972
UPF Net Operating Balance	-237	-42	-331	-132	-188	-257	-218
Economic Inflows/(Outflows)	332	291	303	234	117	93	243
Operating Result	95	247	-28	102	-71	-164	25

As shown below in Chart 1.1, total expenses have exceeded total revenue for the past five financial years.

**Chart 1.1
Total Territory - Operating Result**

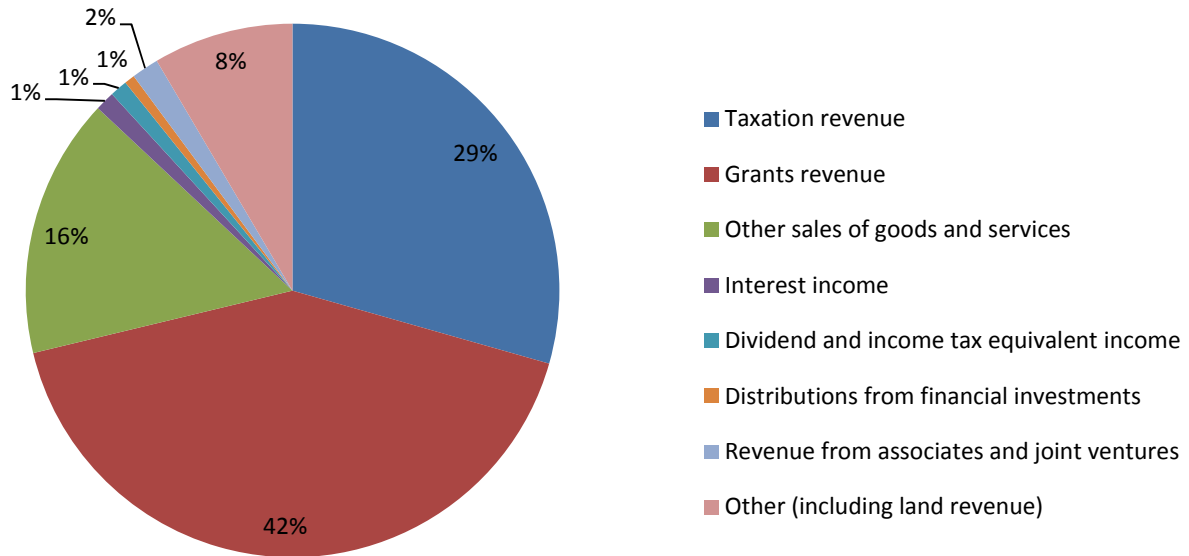


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Revenue

Total Territory revenue for the 2017-18 financial year was \$5,692 million. As demonstrated below in Chart 1.2, the majority of the Territory's revenue is from Grants Revenue (42 per cent) followed by taxation (29 per cent).

**Chart 1.2
Total Territory - Revenue Sources**



Total revenue of \$5,692 million for the 2017-18 financial year was in line with the 2017-18 Budget estimate of \$5,649 million.

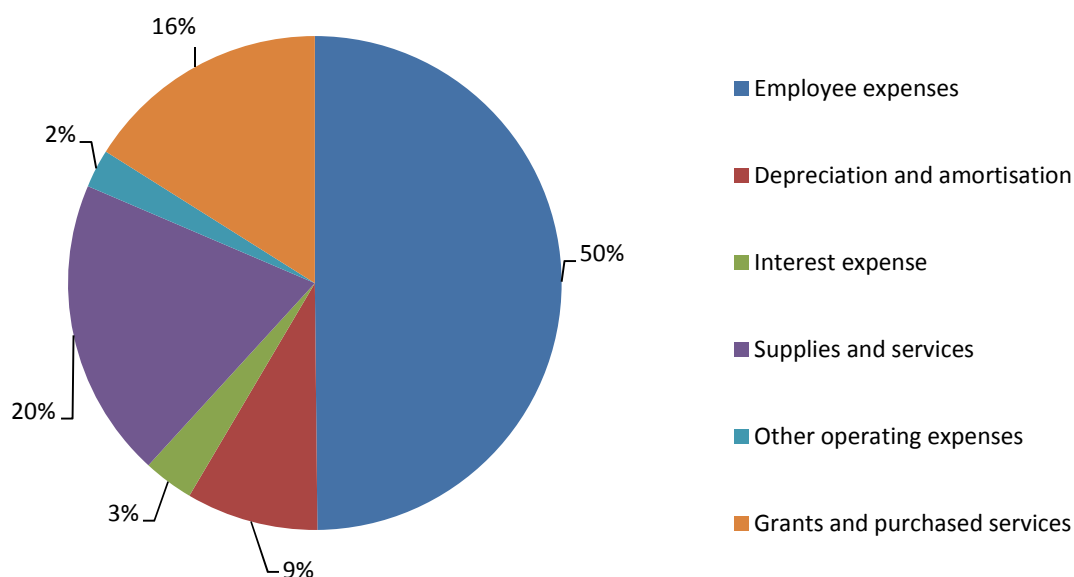
Total revenue in 2017-18 was \$256 million (4.7 per cent) higher than the 2016-17 financial year result of \$5,436 million. This was mainly due to an increase in Commonwealth Government Grants for GST Revenue from revised GST revenue pools, population estimates and recommendations arising from the Commonwealth Grants Commission Report on GST Revenue Sharing Relativities.

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Expenses

Total expenses for the 2017-18 financial year was \$5,734 million. As shown below in Chart 1.3, the largest percentage of the Territory's expenses is employee related costs (50 per cent).

**Chart 1.3
Total Territory - Areas of Expenditure**



Total expenses in 2017-18 of \$5,734 million was \$246 million (4.1 per cent) lower than the 2017-18 Budget estimate of \$5,980 million. This mainly reflects lower supplies and services following a change in the demolition processes under the Public Housing Renewal Taskforce, whereby the developer will now complete demolition in 2018-19 and 2019-20, the Treasurer's Advance not being fully spent and lower expenses for medical supplies due to lower demand for high cost drugs. It also reflects lower other operating expenses due to lower than forecast cost of land sold related to delayed settlements in Throsby and Denman Prospect 2 and lower insurance claims expense.

Total expenses were broadly in-line with the 2016-17 outcome of \$5,673 million.

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Economic Inflows/(Outflows)

The economic inflows/(outflows) for the 2017-18 financial year were a surplus of \$291 million, which is \$41 million lower than the 2016-17 result of \$332 million. This is mainly due to lower gains on non-financial assets and a higher level of inventory write-downs in the Suburban Land Agency.

Financial Position

**Table 2.1
Total Territory - Financial Position**

	2016-17 Actual	2017-18 Actual	2017-18 Annual Budget	2018-19 Annual Budget	2019-20 Forward Estimate	2020-21 Forward Estimate	2021-22 Forward Estimate
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Financial Assets	7,134	7,210	6,727	6,871	7,077	7,433	7,678
Non-Financial Assets	23,809	24,354	24,442	25,650	26,487	26,926	27,126
Total Assets	30,942	31,564	31,169	32,521	33,564	34,359	34,804
Total Liabilities	14,855	15,760	12,791	14,575	15,485	16,146	16,409
Net Assets	16,087	15,804	18,378	17,946	18,080	18,213	18,395
Net Financial Liabilities	8,697	9,553	7,112	8,728	9,446	9,770	9,807
Net Debt (excluding Superannuation related Investments assets/ liabilities)	2,781	2,804	3,447	3,744	4,380	4,631	4,630

Net Assets at 30 June 2018 of \$15,804 million was \$2,574 million (14.1 per cent) lower than the 2017-18 Budget estimate of \$18,378 million, and \$283 million (1.8 per cent) lower than the 2016-17 result of \$16,087 million.

Net Financial Liabilities, which include net debt and superannuation liabilities at 30 June 2018, were \$9,553 million which is \$2,441 million (34.3 per cent) higher than the 2017-18 Budget estimate of \$7,112 million and \$856 million (9.8 per cent) higher than the 30 June 2017 result of \$8,697 million. These variances are mainly due to the change in the estimated defined benefit superannuation liability at 30 June 2018. This estimate is based on a discount rate of 3.11 per cent, compared to 3.51 per cent at 30 June 2017, and a long-term assumption of 6 per cent in the 2017-18 Budget.

Net Debt (Excluding Superannuation Related Investments assets/liabilities) takes into account gross debt liabilities as well as financial assets (such as cash reserves and investments). Net Debt is calculated as the sum of deposits held, advances received and borrowings, less the sum of cash and deposits, advances paid, investments, loans and placements. Superannuation investments assets and liabilities have been excluded in determining Net Debt.

Note (a): In accordance with the requirements of AASB 119 the superannuation liability valuation must be based on the Commonwealth Government Bond rate. This rate has decreased over the 2017-18 financial year. A lower discount rate increases the present value estimate of the superannuation liability.

The Budget superannuation liability valuation estimate uses a long-term set of financial and demographic assumptions, including the use of a long-term discount rate assumption, in order to maintain a consistent approach to the presentation of the superannuation liability estimate.

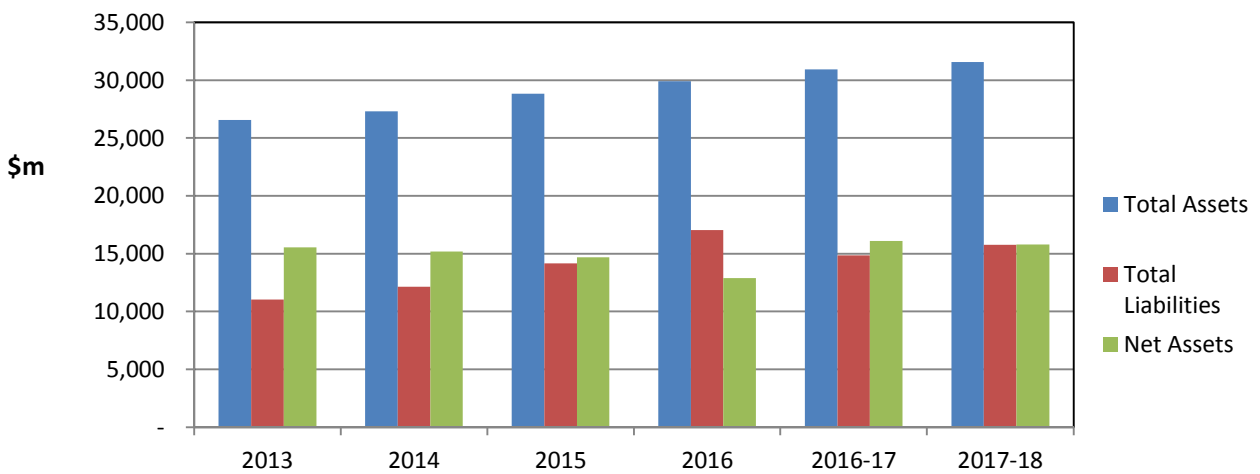
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Financial Position - Continued

Net Debt at 30 June 2018 of \$2,804 million was broadly in line with the 30 June 2017 result of \$2,781 million, and was \$643 million (18.7 per cent) lower than the 2017-18 Budget estimate of \$3,447 million. This was mainly due to an increase in the receipt of Commonwealth Government payments for GST and the ACT Healthy Waterways Project, receipts for the Renewable Energy Innovation fund and Next Generation Energy Storage Program and sales under the Loose-fill Asbestos Insulation Eradication Scheme and lower capital works expenditure.

Chart 2.1 below demonstrates the Territory's Balance Sheet (Actuals) over time.

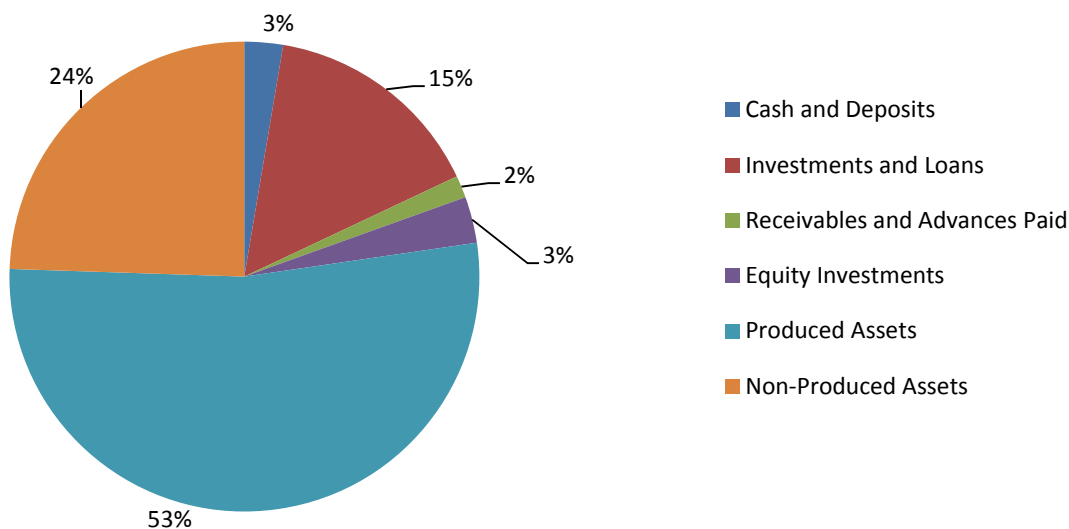
**Chart 2.1
Total Territory - Balance Sheet**



Assets

Total assets at 30 June 2018 was \$31,564 million. As can be seen from Chart 2.2 below, the majority of the Territory's assets are produced assets (53 per cent) - specifically property, plant and equipment.

**Chart 2.2
Total Territory - Asset Types**



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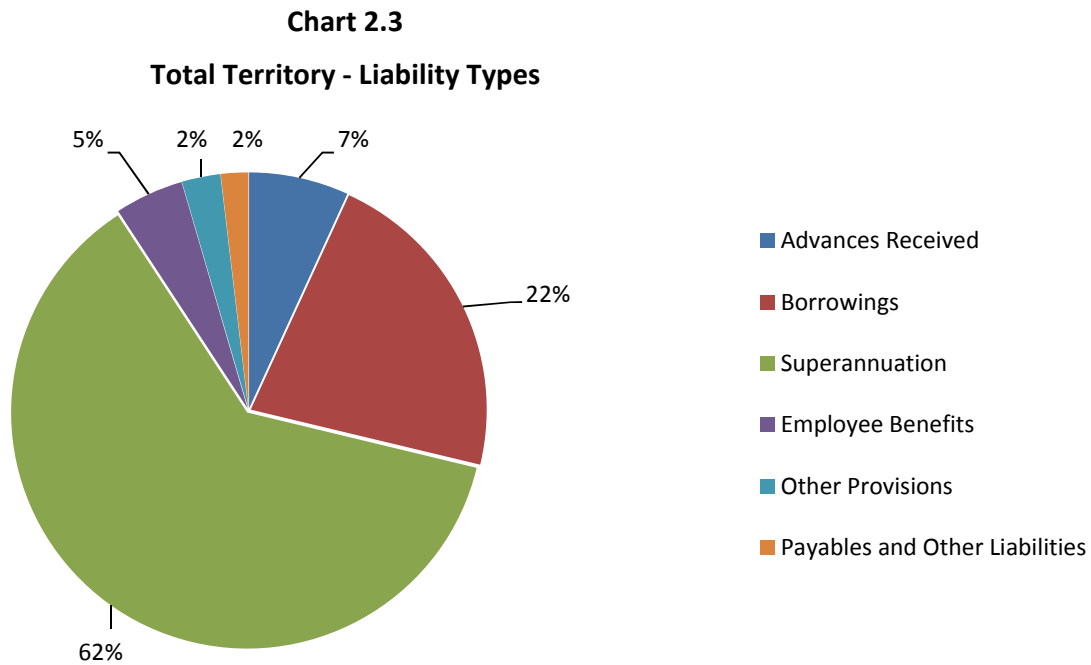
Assets - Continued

Total assets at 30 June 2018 of \$31,564 million was \$395 million (1.3 per cent) higher than the 2017-18 Budget estimate of \$31,169 million.

At 30 June 2018, total assets increased slightly by \$622 million (2.0 per cent) from \$30,942 million compared to 30 June 2017.

Liabilities

Total Liabilities at 30 June 2018 was \$15,760 million. As can be seen from Chart 2.3 below, the majority of the Territory's liabilities are related to superannuation (62 per cent).



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Liabilities - Continued

Total Liabilities at 30 June 2018 increased by \$2,969 million (23.2 per cent) from the 2017-18 Budget estimate of \$12,791 million. This was mainly due to a higher than budgeted superannuation liability arising from the use of a lower discount rate of 3.11 per cent used to estimate the present value of the superannuation liability compared to the current long-term average budget estimate of 6 per cent.

Total liabilities of \$15,760 million at 30 June 2018 increased by \$905 million (6.1 per cent) compared to the 30 June 2017 result of \$14,855 million. This was mainly due to the increase in the estimated value of the superannuation liability explained above. The discount rate in 2016-17 was 3.51 percent.

While the unfunded superannuation position is significant, the defined benefit schemes (CSS and PSS) to which the liability relates is closed to new members. All superannuation liabilities incurred for new employees since 1 July 2005 are fully funded through accumulation scheme arrangements.

In relation to the unfunded liability, the Government maintains, as a key financial objective, a funding plan to extinguish the Territory's unfunded defined benefit superannuation liability by 2030.

Cash Flows

**Table 3.1
Total Territory - Cash Flow Position**

	2016-17 Actual	2017-18 Actual	2017-18 Annual Budget	2018-19 Annual Budget	2019-20 Forward Estimate	2020-21 Forward Estimate	2021-22 Forward Estimate
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Net Cash Flows from Operating Activities	596	556	470	573	354	608	589
Net Cash Flows from Investments in Non-Financial Assets	-460	-519	-703	-607	-896	-746	-466
Cash Surplus (+) / Deficit (-)	136	38	-234	-34	-542	-138	124

Net Cash Flows from Operating Activities was \$556 million, which is \$86 million (18.3 per cent) more than the 2017-18 Budget estimate of \$470 million and \$40 million (6.7 per cent) lower than the 2016-17 outcome of \$596 million. The higher than 2017-18 Budget estimate is mainly due to lower payments for goods and services. The lower than 2016-17 outcome is mainly due to higher payments for employee expenses and goods and services.

Net Cash Flows from Investments in Non-Financial Assets of -\$519 million was \$184 million (26.1 per cent) lower than the 2017-18 Budget estimate of -\$703 million and \$59 million (12.8 per cent) higher than the 2016-17 outcome of -\$460 million. The lower than estimated outflows are mainly due to the deferral of capital works expenditure for projects such as the Canberra Hospital Re-Development being adjusted for detail design and planning work to facilitate construction activities, the deferral of Light Rail Stage 1 project funding to 2018-19 as funding was not required in 2017-18 and re-profiling the purchases of land for the Land Rent Scheme due to lower sales of land. The higher than 2016-17 outcome is mainly due to higher capital works payments.

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**Table 4.1
Total Territory - Infrastructure Program**

	2016-17 Actual ^(a)	2017-18 Actual	2017-18 Annual Budget	2018-19 Forward Estimate	2019-20 Forward Estimate	2020-21 Forward Estimate	2021-22 Forward Estimate
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Capital Works Program	513	657	888	746	605	187	96

The 2017-18 Whole-of-Government Capital Works Program Investment for the Territory was \$657 million; this was \$231 million (26.0 per cent) less than the 2017-18 Annual Budget of \$888 million.

Major infrastructure investment during 2017-18 included (project spend):

Better Public Housing – New public housing properties (\$121 million);
 University of Canberra Public Hospital (\$47 million);
 Better schools for our kids – Public school infrastructure upgrades (\$19 million);
 Caring for our Environment – Water Quality Improvement – Contributions to the ACT Healthy Waterways Project (\$19 million);
 Better Health Services – Upgrading and maintaining ACT Health assets (\$16 million);
 Better Roads for Gungahlin – Horse Park Drive duplication (Mulligans Flat Road to the Federal Highway) (\$16 million);
 Better Roads for Weston Creek – Cotter Road duplication (Tuggeranong Parkway to Yarralumla Creek) (\$14 million);
 Better schools for our kids – Narrabunda College and Campbell Primary School (\$13 million);
 Better support when it matters – Public Housing Renewal – New and better properties (\$12 million);
 Better Road for Tuggeranong – Ashley Drive duplication – Stage 2 (\$12 million);
 Schools for the Future – North Gungahlin and Molonglo (\$12 million);
 Schools for the Future – Modernising Belconnen High (\$12 million);
 Light Rail – Stage 2 – Procurement and delivery (\$11 million);
 Better Roads for Gungahlin – Gundaroo Drive duplication – Stage 1 (\$11 million);
 Better Schools – Investment in Gungahlin school infrastructure (\$11 million); and
 University of Canberra Public Hospital Car Park (\$10 million).

Major infrastructure physically completed during 2017-18 included (total funded project value):

University of Canberra Public Hospital (\$200 million);
 Majura Parkway to Majura Road – Link road (\$15 million);
 Molonglo 2 – Water Supply, Trunk Sewer and Stormwater Infrastructure – Stage 1 (\$10 million);
 Schools for the Future – Caroline Chisholm School – Centre for Innovation and Learning (\$6 million); and
 Urban Renewal Program – Phillip Oval upgrade (\$5 million).

During 2017-18, there was continued progress on the Public Private Partnerships (PPP) for the ACT Law Courts Facilities and the Light Rail Stage 1 Project. These PPPs are long-term contracts entered into between the Territory and a private sector consortium (the operator) to design, finance, construct and operate/maintain these assets over a concessional term.

Note: (a) The 2017-18 Capital Works Program included information technology and plant and equipment projects for the first time.