1.2 FISCAL STRATEGY – FINANCIAL OBJECTIVES AND KEY MEASURES

Fiscal Strategy

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

In the 2012-13 Budget, the Government has reverted to its original target of returning to surplus in 2015-16.

Since 2010-11, the Territory's economy has continued to moderate. In 2012-13, economic growth is forecast to moderate due to the Commonwealth Government's stronger fiscal consolidation and softening of own source revenues.

The Government has accepted a temporary deterioration in the operating position in order to maintain reasonable levels of expenditure and investment.

In the context of a moderating economy and Commonwealth contraction in expenditure, the focus is on supporting the economy, jobs and services to the community.

The Government continues to maintain its fiscal strategy, which has been successful in ensuring that priority services are sustainable.

The financial objectives and key measures of this strategy 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 1 per cent per annum.

New expenditure initiatives in this Budget are fully offset by savings.

Further information on the Budget Plan is provided in 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. In 2011-12, the Plan was updated to target a surplus by 2013-14. Due to the change in the economic and financial circumstances, the Budget has reverted back to the original 2015-16 target.

The Net Operating Balance for the Budget is estimated to be in deficit of $318.3 million, with a forecast deficit position until 2015-16. This is due to a number of factors including:

- lower dividends from the Public Trading Enterprise (PTE) sector mainly driven by moderation of commercial activities related to land supply and development;
- moderation in the housing market; and
- higher employee expenses associated with revised wage parameters.

The Headline Net Operating Balance is expected to return to surplus by 2015-16, largely due to expenditure growth constrained at 4 per cent and forecast growth in revenues at 4¾ per cent.

Table 1.2.1
The Budget Operating Surplus/Deficit

	2011-12 Est.Outcome $m	2012-13 Budget $m	2013-14 Estimate $m	2014-15 Estimate $m	2015-16 Estimate $m
UPF Net Operating Balance	**-133.0**	**-395.7**	**-217.1**	**-143.3**	**-71.8**
Plus: Expected Long Term Capital Gains on superannuation Investments[1]	7.4	77.4	86.8	92.0	97.0
Headline Net Operating Balance	**-125.5**	**-318.3**	**-130.2**	**-51.3**	**25.2**

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[1].

This is a significant matter for the ACT as the long term capital gains on superannuation investments range from $77.4 million in 2012-13 to $97 million in 2015-16.

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+

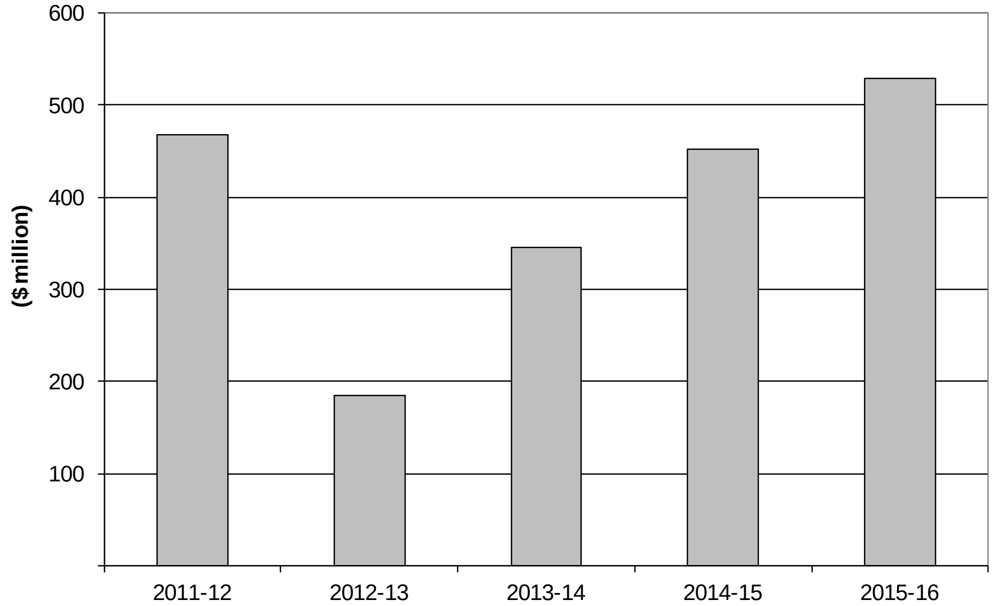
1. State governments have typically injected assets into their public sector superannuation schemes to partly fund those schemes. Under Australian Accounting Standard 119, *Employee Benefits*, the expected rate of return on these assets can be subtracted in determining the total superannuation expense 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.dtf.vic.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.

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 $184.9 million in 2012-13, with surplus balances across the forward estimates. A revised operating cash surplus of $467.3 million is estimated for 2011-12. 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's Balance Sheet continues to be one of the strongest of any Australian government. Measures announced in past budgets and continued in the 2012-13 Budget, combined with the 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.

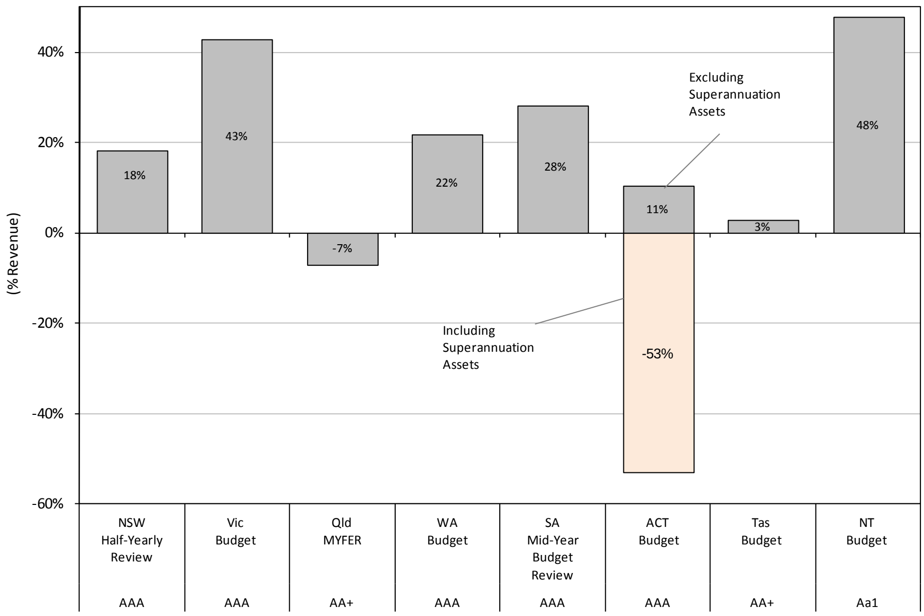
Net Debt

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 positive General Government Sector net debt in 2012-13. This indicates that the Territory's General Government Sector cash reserves and investments are lower than gross debt liabilities.

The figures below have been sourced from other jurisdictions' Budget documentation as indicated.

Figure 1.2.2
Net Debt to Revenue Ratio General Government Sector: 2012-13



Source: The interjurisdictional data utilised in this comparison is taken from each jurisdiction's most current Budget documentation. Differing sources have been employed as not all jurisdictions have released their 2012-13 Budgets.

Net Financial Liabilities

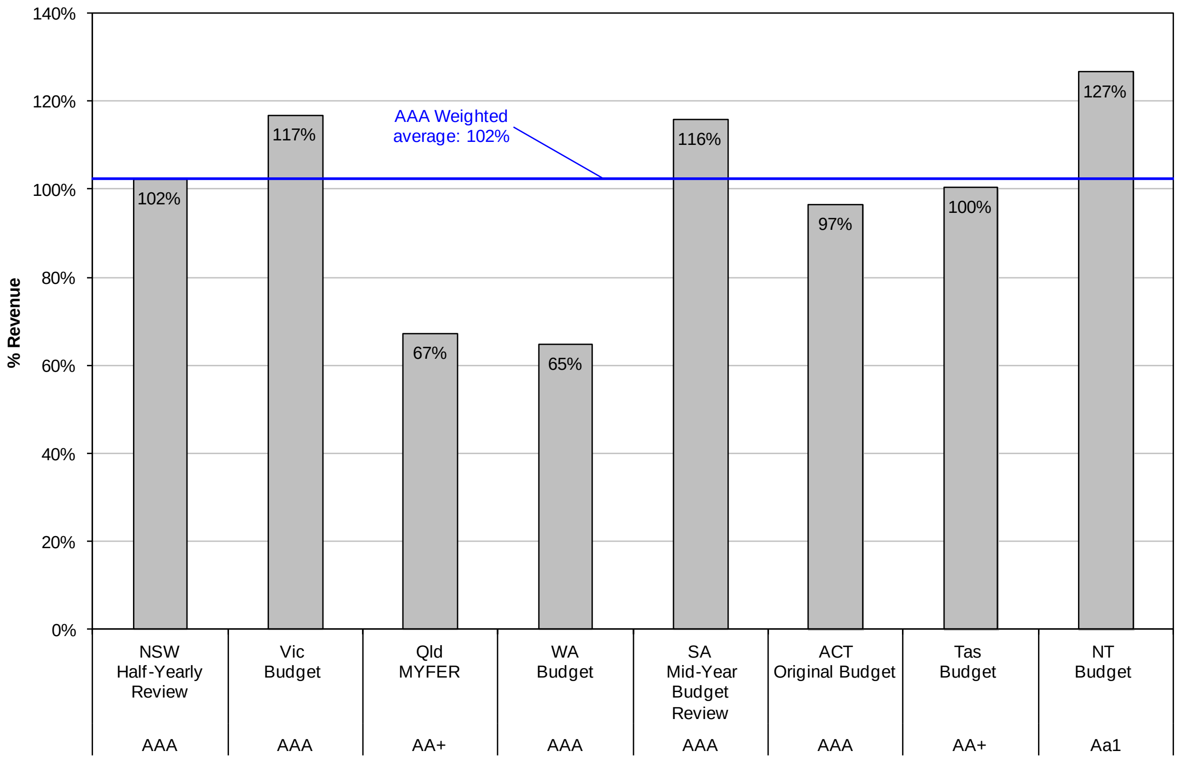
Net financial liabilities are a broad measure of General Government Sector liabilities, including net debt and superannuation liabilities. The net financial liability has increased to 97 per cent in 2012-13, compared to 64 per cent in the 2011-12 Budget, largely due to the increased valuation of superannuation liabilities. Despite this increase, the ACT 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 each jurisdiction's most current Budget documentation.

Figure 1.2.3 below compares the ACT's net financial liabilities as a proportion of revenue with other jurisdictions. The ACT also continues to remain below the weighted average for other AAA rated jurisdictions.

Figure 1.2.3
Net Financial Liabilities to Revenue Ratio General Government Sector: 2012-13



Source: The interjurisdictional data utilised in this comparison is taken from each jurisdiction's most current Budget documentation. Differing sources have been employed as not all jurisdictions have released their 2012-13 Budgets.

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.

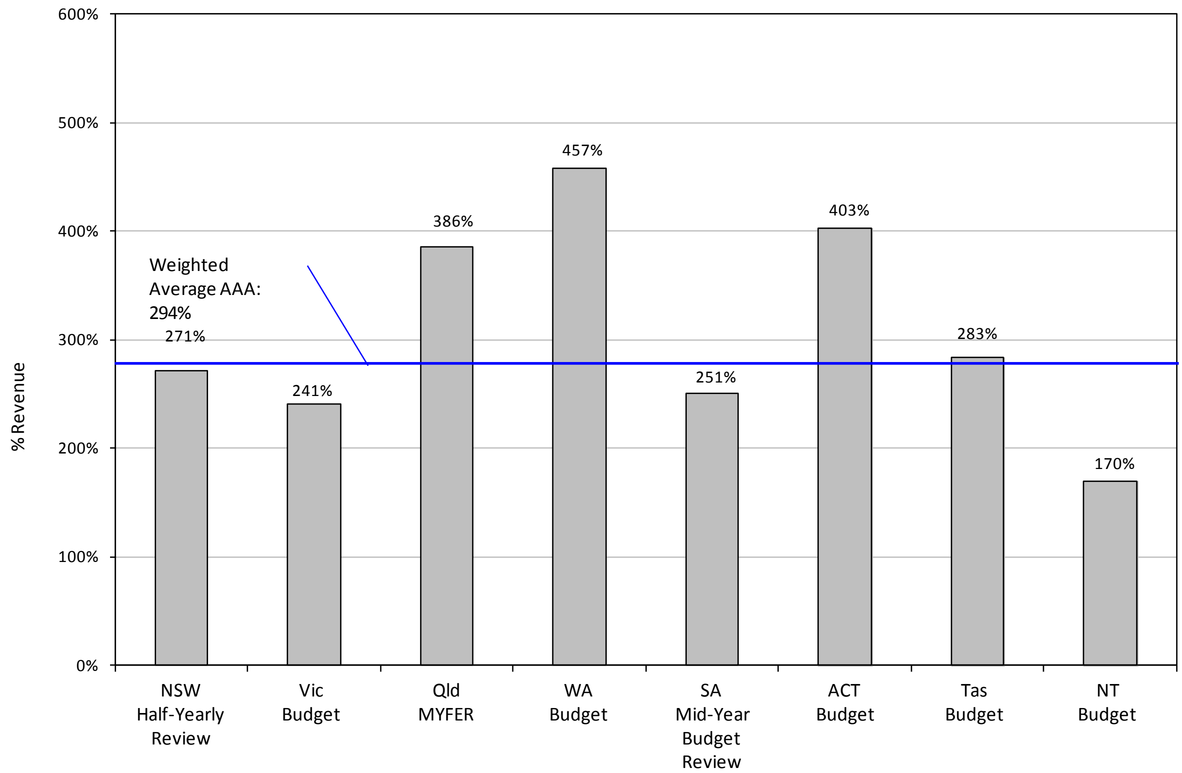
The Government's objective is to maintain this ratio within the range of all AAA rated jurisdictions in Australia. While this ratio is subject to volatility (in particular, net financial liabilities can fluctuate, sometimes substantially, depending on the condition of financial markets), it is desirable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

The 2012-13 Budget anticipates new general government sector borrowing for capital purposes of up to $790 million over 2012-13 to 2013-14. It is estimated that $490 million borrowings will be repaid by the end of 2015-16 reflecting only a short term need for additional borrowings. The infrastructure investment funded by this debt will assist the ACT economy, consumer confidence, and enhance service delivery for ACT residents.

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: 2012-13



Source: The interjurisdictional data utilised in this comparison is taken from each jurisdiction's most current Budget documentation. Differing sources have been employed as not all jurisdictions have released their 2012-13 Budgets.