

PART 4: DEVELOPMENTS IN THE CONSOLIDATED NON-FINANCIAL PUBLIC SECTOR

The fiscal and cash balances of both levels of government are expected to remain in deficit in 2011-12 but improve over the forward estimates.

The improvement in the fiscal indicators reflects the withdrawal of economic stimulus spending and, in future years, the expected recovery in revenue collections from the effects of the global recession.

The Commonwealth is estimated to return to a surplus in 2012-13 but continued deficits in some States result in consolidated fiscal deficits continuing though to 2013-14.

INTRODUCTION

This Part provides a framework in which to consider developments in the Commonwealth's Budget through consideration of the fiscal position of all Australian governments.

It discusses trends in key fiscal indicators including net operating balance, fiscal balance, cash balance, net debt and net interest payments, at the Commonwealth and State and local levels, and together at the consolidated level.

The Part focuses on trends in the non-financial public sector (NFPS) which is comprised of the general government sector and the public non-financial corporations (PNFC) sector. The general government sector provides non-market goods and services such as policing, health and education. The PNFC sector comprises government-controlled corporations engaged in providing market goods such as electricity and public transport, but not financial services.

For further information on the fiscal indicators and the institutional structure of the public sectors see Budget Paper No. 1, Statement 9.

The state estimates in this part come from 2010-11 mid-year financial reports with the exception of Victoria, the Australian Capital Territory and the Northern Territory, which are drawn from 2011-12 Budgets.

Additional data tables can be found in Appendix E.

NET OPERATING BALANCE

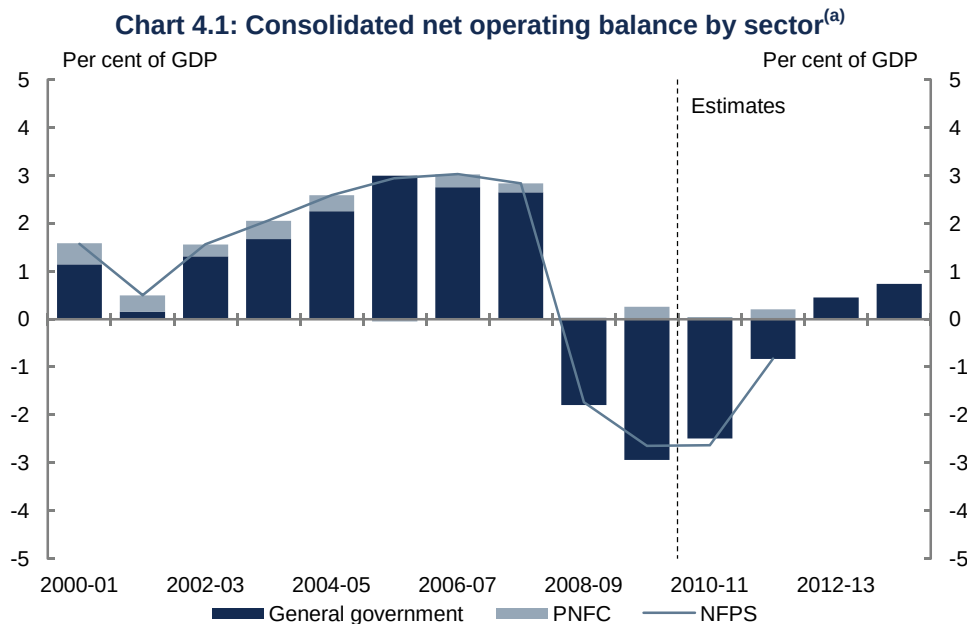
The net operating balance measures, in accrual terms, the gap between recurrent expenses and revenue for a given period. This is the headline measure used by most States and provides an indication of the medium-term sustainability of the existing level of government services. The Commonwealth does not use net operating balance as a headline fiscal indicator.

In aggregate, the states are estimating operating deficits in 2011-12 and the forward years, with the size of the operating deficits decreasing over time. However, while in aggregate the States are in operating deficit, the circumstances in individual states vary.

New South Wales, Victoria, Western Australia, South Australia and the Northern Territory are estimating operating surpluses in 2011-12. These states, with the exception of the Northern Territory, are also forecasting operating surpluses through to 2013-14.

Queensland, Tasmania and the Australian Capital Territory are estimating operating deficits in 2011-12. The deficits are expected to continue to 2013-14. Queensland's deficit is partly due to expenditure associated with the recent natural disasters.

As shown in Chart 4.1, the consolidated general government net operating position is estimated to be in deficit in 2011-12, returning to a surplus of 0.5 per cent of GDP in 2012-13.



(a) Data for the PNFC sector (and therefore NFPS) are not available beyond 2011-12.

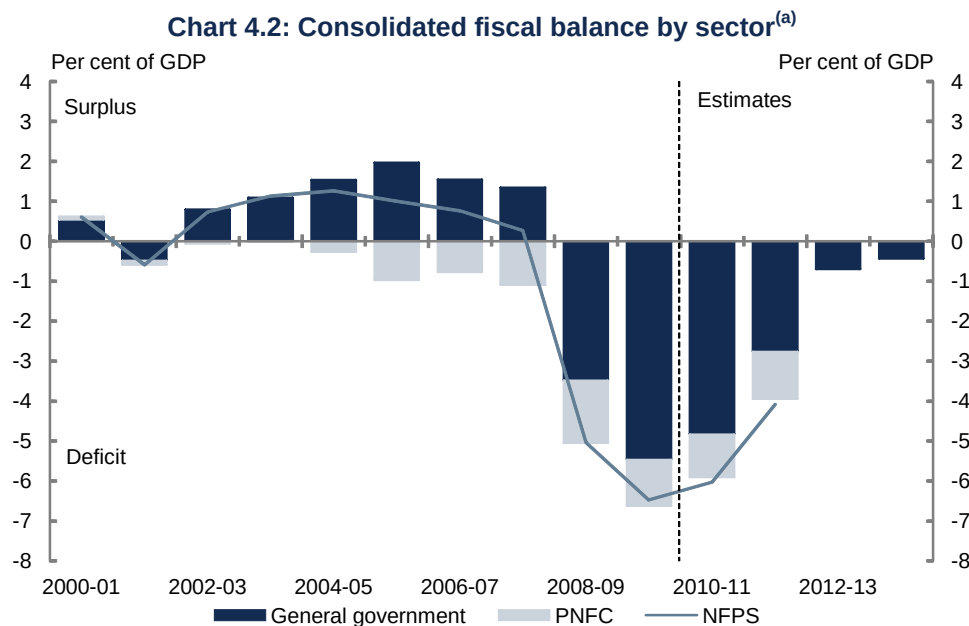
FISCAL AND CASH BALANCES

A fiscal surplus indicates that a government is saving more than enough to finance all of its investment spending and is therefore not contributing directly to the current account deficit. A fiscal deficit indicates that a government needs to borrow or liquidate financial assets in order to fund its capital and/or recurrent expenditures.

As the fiscal balance includes capital transfers and investment in non-financial assets, which are not included in the net operating balance, the difference between the fiscal balance and the net operating balance is the effect of investment in infrastructure.

The fiscal balances of both the Commonwealth and state/local general government sectors are expected to improve as economic stimulus spending is withdrawn and, in future years, revenue collections recover from the effects of the global recession. The Commonwealth general government sector is expected to return to a surplus in 2012-13 but continued deficits in some States result in consolidated general government fiscal deficits over the forward years.

As shown in Chart 4.2, the consolidated general government sector fiscal balance is expected to be a deficit of 4.8 per cent of GDP in 2010-11 and 2.8 per cent of GDP in 2011-12. Fiscal deficits are also expected in the PNFC sector, leading to an NFPS deficit of 6.0 per cent of GDP in 2010-11 and 4.1 per cent of GDP in 2011-12.

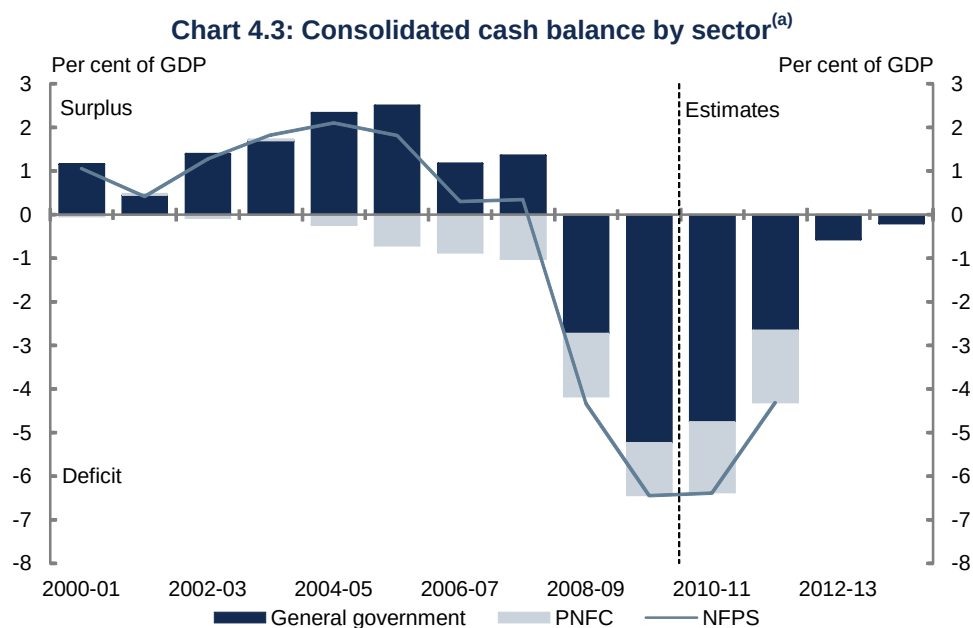


(a) Data for the PNFC sector (and therefore NFPS) are not available beyond 2011-12.

The cash balance is the equivalent of a fiscal balance measured on a non-accrual basis, that is, capturing payments and receipts as they occur. It therefore reflects the extent to which cash is available to a government.

The same trends discussed above in relation to the fiscal balance are also affecting the cash balances of both the Commonwealth and state/local governments.

As shown in Chart 4.3, the consolidated general government sector cash balance is expected to be a deficit of 4.8 per cent of GDP in 2010-11 and 2.7 per cent of GDP in 2011-12. Cash deficits are also expected in the PNFC sector, leading to an NFPS deficit of 6.4 per cent of GDP in 2010-11 and 4.3 per cent of GDP in 2011-12.



(a) Data for the PNFC sector (and therefore the NFPS) are not available beyond 2011-12.

NET DEBT

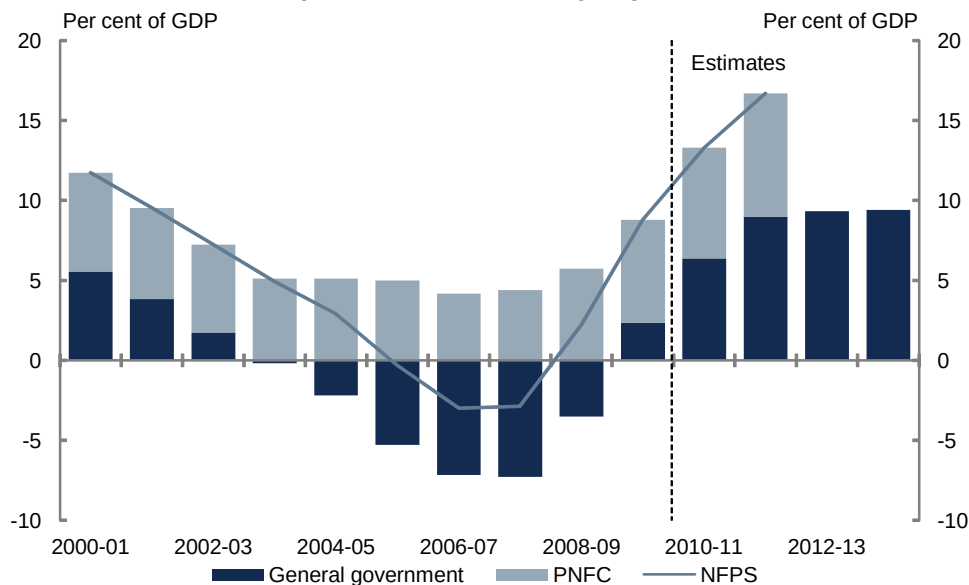
Net debt is the sum of selected financial liabilities (deposits held, advances received, government securities, loans and other borrowing) less the sum of selected financial assets (cash and deposits, advances paid, investments, loans and placements). Net debt does not include superannuation-related liabilities.

General government sector net debt is expected to be 9.0 per cent of GDP in 2011-12.

General government sector net debt for the Commonwealth is forecast to peak in 2011-12, and decline over the forward years as the fiscal surpluses from 2012-13 allow the repayment of debt. State/local sector net debt is expected to increase in 2011-12 reflecting the aggregate net operating balance deficits of the states and their investment in infrastructure.

In the NFPS sector, net debt is expected to be 16.7 per cent of GDP in 2011-12 (Chart 4.4).

**Chart 4.4: Consolidated net debt by sector
(as at end of financial year)^(a)**



(b) Data for the PNFC sector (and therefore the NFPS) are not available beyond 2011-12.

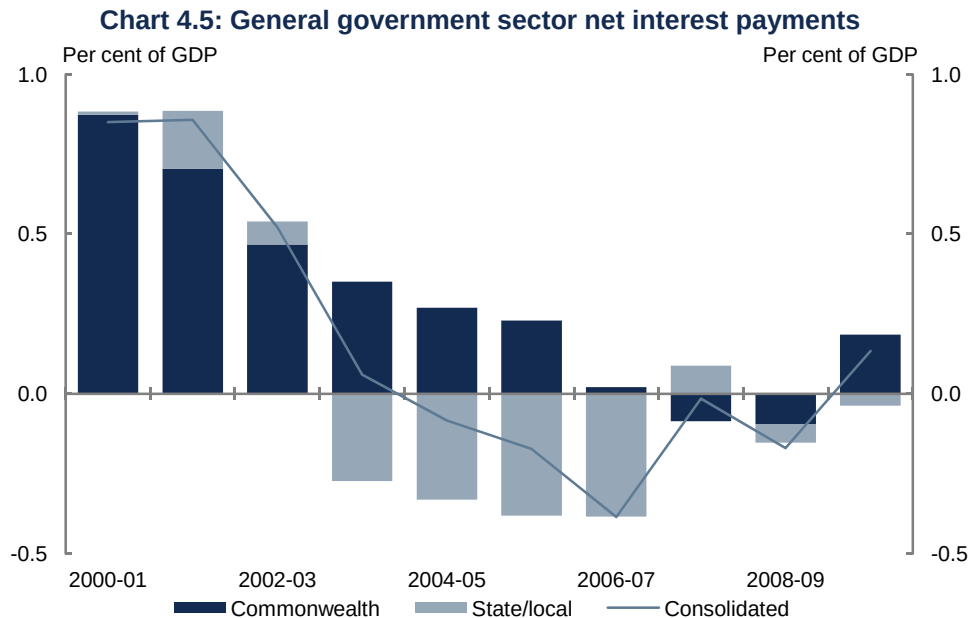
While the States estimate net debt in the PNFC sector over the forward years, the Commonwealth does not. A majority of the States are projecting PNFC net debt (and therefore the NFPS) to continue to increase over the forward years, with NFPS net debt of the States reaching 10.5 per cent of GDP in 2013-14.

NET INTEREST PAYMENTS

Net interest payments reflect the cost of servicing debt. The higher the net debt of a government, the greater the call that will be imposed on a government's future revenue flows to service that debt.

Consolidated general government sector net interest payments have declined since 2001-02 and reached a low in 2006-07, as the Commonwealth and state/local general government sectors experienced sustained budget surpluses, which were used, in part, to pay down debt.

In 2009-10, consolidated general government sector net interest payments rose by 0.3 percentage points of GDP, reflecting increased net debt as a result of the global recession.



THE AUSTRALIAN LOAN COUNCIL

The Australian Loan Council is a Commonwealth-State ministerial council that coordinates public sector borrowing. The Loan Council consists of the Prime Minister of Australia and the Premier/Chief Minister of each State and Territory. In practice, each member is represented by a nominee, usually the Treasurer of that jurisdiction, with the Commonwealth Treasurer as Chair.

Current Loan Council arrangements operate on a voluntary basis and emphasise transparency of public sector financing rather than adherence to strict borrowing limits. These arrangements are designed to enhance financial market scrutiny of public sector borrowing and facilitate informed judgments about each government's financial performance.

The Loan Council traditionally meets annually around March or April to consider jurisdictions' nominated borrowings for the forthcoming year. As part of the agreed arrangements, the Loan Council considers these nominations, having regard to each jurisdiction's fiscal position and the macroeconomic implications of the aggregate figure.

Since 2009-10, the role of the Loan Council has expanded to include reporting on the macroeconomic implications of proposed expenditure from the Building Australia Fund, the Health and Hospitals Fund and the Education Investment Fund.

The Loan Council also provides an additional level of scrutiny regarding the use of the Guarantee of State and Territory Borrowing introduced during the global financial crisis and which closed to new issuance on 31 December 2010.

Outcome of the 2011 Loan Council meeting

The Loan Council met on 7 April 2011 to consider Loan Council Allocation nominations for 2011-12. The Loan Council approved each jurisdiction's nominated allocation. In aggregate, the nominations represent a deficit of \$46.7 billion (Table 4.1). The States nominated a deficit of \$32.5 billion and the Commonwealth nominated a deficit of \$14.2 billion.

The Commonwealth's 2011-12 Loan Council Allocation budget update is available in Budget Paper No. 1, Statement 9, Appendix B.

State 2011-12 Loan Council Allocation budget updates will be available in the States' 2011-12 Budgets.

The Loan Council considered the macroeconomic implications of infrastructure spending and found that the Government's fiscal stimulus packages have continued to support the level of economic activity in 2010 and beyond. However, they are detracting from growth as the level of stimulus declines over time. Given the size and

Budget Paper No. 3

likely timing profile of any spending on new projects, the Loan Council determined that the drawdown of the remaining balances in the Nation Building Funds is not likely to have a material impact on aggregate demand and on the level of spare capacity in the economy.

The Loan Council determined that the Guarantee was being used to support state infrastructure investment and was not being used inappropriately to finance lending to non-government entities or to purchase other financial assets.

As at 31 March 2011, the face value of state and territory borrowings covered by the Guarantee was \$50.8 billion, down from \$62.0 billion at 30 September 2010.

Table 4.1: Loan Council Allocation nominations for 2011-12^(a)

	NSW	VIC	QLD	WA	SA	TAS	ACT	NT	Cwth	Total
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Nominated 2011-12 LCAs										
General government sector cash surplus(-)/deficit(+)	1,474	607	7,406	1,126	909	235	48	334	9,501	
PNFC sector cash surplus(-)/deficit(+)	3,362	2,692	3,096	1,834	-366	331	233	217	-101	
Non-financial public sector cash surplus(-)/deficit(+)(b)	4,836	3,319	10,503	2,959	543	566	280	551	9,400	
Acquisitions under finance leases and similar arrangements	848	5,279	82	8	0	0	0	0	17	
<i>equals</i> ABS GFS cash surplus(-)/deficit(+)	5,684	8,598	10,585	2,967	543	566	280	551	9,417	
<i>minus</i> Net cash flows from investments in financial assets for policy purposes(c)	-163	5	-87	0	10	-4	-7	0	-5,577	
<i>plus</i> Memorandum items(d)	56	666	2,176	75	-566	34	-8	0	-761	
Loan Council Allocations	5,903	9,260	12,848	3,043	-33	603	279	551	14,233	46,687
2011-12 tolerance limit(e)	1,544	1,019	1,011	802	333	157	93	105	7,077	

(a) Loan Council Allocation (LCA) nominations for 2011-12 reflect best estimates of cash surpluses/deficits. Nominations have been provided on the basis of policies announced up to and included in jurisdictions' mid-year financial reports and the Commonwealth's *Mid-Year Economic and Fiscal Outlook 2010-11*. Each jurisdiction will publish an updated LCA estimate as part of its budget documentation.

(b) The sum of the deficits of the general government and PNFC sectors may not directly equal the non-financial public sector surplus due to intersectoral transfers.

(c) Net cash flows from investments in financial assets for policy purposes comprise net lending by governments with the aim of achieving government policy as well as net equity sales and net lending to other sectors or jurisdictions. Such transactions involve the transfer or exchange of a financial asset and are not included within the cash deficit. However, these flows have implications for a government's call on financial markets. Net cash flows from investments in financial assets for policy purposes are displayed with the same sign as reported in cash flow statements.

(d) Memorandum items are used to adjust the NFPS surplus/deficit to include in LCAs certain transactions — such as operating leases — that have many of the characteristics of public sector borrowings but do not constitute formal borrowings. They are also used, where appropriate, to deduct from the NFPS surplus/deficit certain transactions that the Loan Council has agreed

(e) should not be included in LCAs, for example, the funding of more than employers' emerging costs under public sector superannuation schemes, or borrowings by entities such as statutory marketing authorities. Where relevant, memorandum items include an amount for gross new borrowings of government home finance schemes.

(f) Tolerance limits are designed, inter alia, to accommodate changes to LCAs resulting from changes in policy. Tolerance limits apply between jurisdictions' LCA nominations and budget estimates, and again between budget estimates and outcomes. They are calculated as 2 per cent of NFPS cash receipts from operating activities in each jurisdiction.

