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

INTRODUCTION

This Part provides a perspective on the financial position of all levels of government in Australia.

It discusses trends in key fiscal indicators including the net operating balance, fiscal balance, cash balance and net debt, at the Commonwealth level, state and territory (state) level, and the consolidated level, which includes local government.

This Part focuses on trends in the non-financial public sector (NFPS) which comprises the general government sector and the public non-financial corporations (PNFC) sector.[1] 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, *Budget Strategy and Outlook 2015-16, Statement 9: Australian Government Budget Financial Statements*.

State estimates in this Part come from their most recent publicly available financial reports. Victoria's and the Northern Territory's estimates are based on their 2015-16 budgets, while the remaining jurisdictions are drawn from their 2014-15 mid-year financial reports. Aggregate state data are only available to 2017-18, so references to the forward estimates in this Part relate to the period 2015-16 to 2017-18.

Additional data tables can be found in Appendix C (available online).

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 budget measure used by most states to provide 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.

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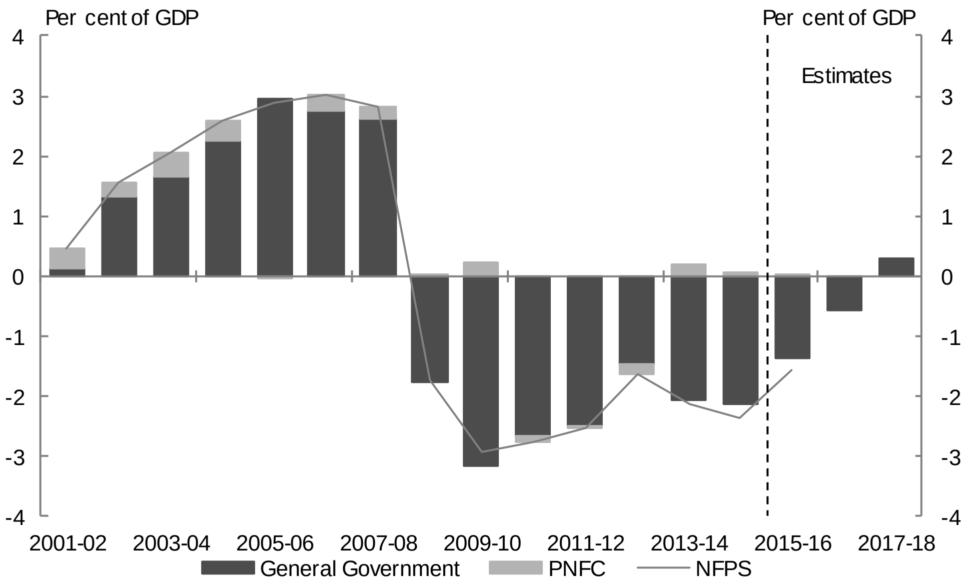
1 Due to inter-sectoral transfers, NFPS does not always equal the sum of the general government and PNFC sectors.

In aggregate, the states are expecting the general government sector to record a net operating surplus of 0.2 per cent of GDP in 2015-16, improving to a surplus of 0.4 per cent of GDP in 2017-18.

In aggregate, on average across the forward estimates, the states are expecting revenue as a proportion of GDP to be 14.2 per cent, which is slightly below the pre-Global Financial Crisis 10-year average of 14.3 per cent of GDP.

As shown in Chart 4.1, the consolidated general government sector is expected to record a net operating deficit of 1.4 per cent of GDP in 2015-16, improving to a surplus of 0.3 per cent of GDP in 2017-18.

Chart 4.1: Consolidated net operating balance by sector[(a)]



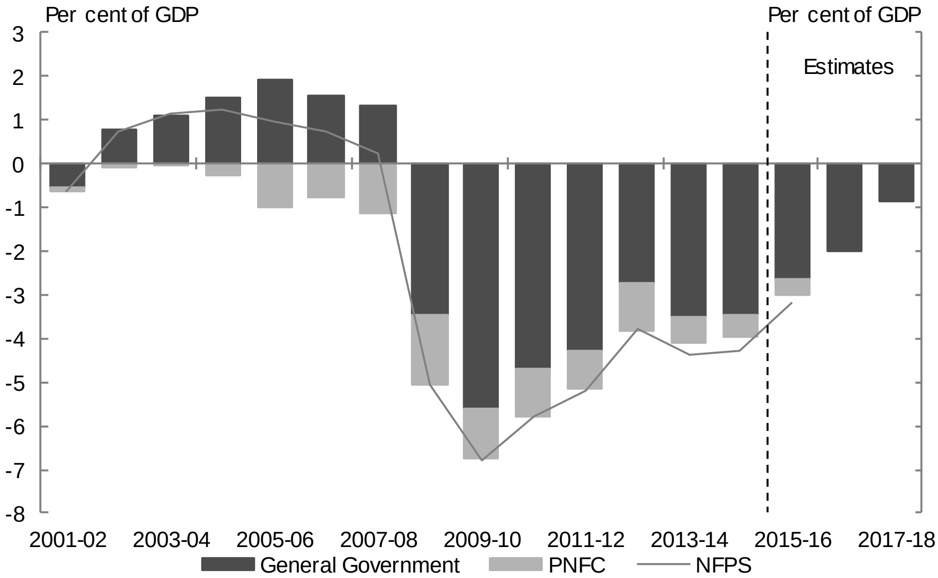
(a) Data for the PNFC sector (and therefore NFPS) are not available beyond 2015-16.

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 non-financial assets, including infrastructure.

Chart 4.2: Consolidated fiscal balance by sector[(a)]



(a) Data for the PNFC sector (and therefore the NFPS) are not available beyond 2015-16.

The fiscal balance of the Commonwealth general government sector is expected to remain in deficit over the forward estimates, however the 2015-16 deficit of 2.0 per cent of GDP is expected to decrease in both 2016-17 and 2017-18.

Aggregate state net capital investment is forecast to increase from 0.5 per cent of GDP in 2015-16 to 0.7 per cent of GDP in 2016-17, before declining to 0.4 per cent of GDP in 2017-18. Despite the improvements in forecast general government state net operating balances over the forward estimates, the aggregate state fiscal balance is expected to remain in deficit until 2016-17, before becoming broadly balanced in 2017-18.

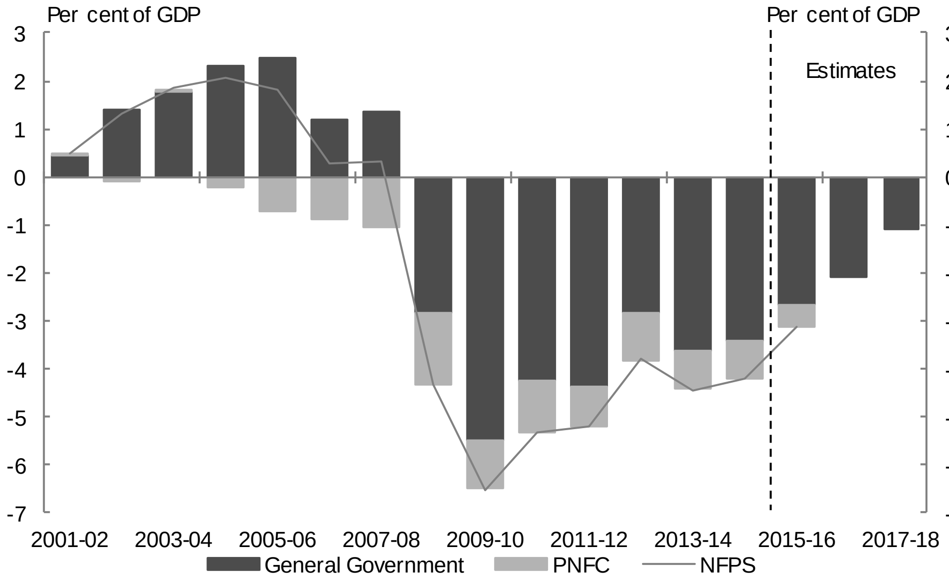
At the consolidated level, the general government sector fiscal balance is expected to remain in deficit across the forward estimates, although the deficit is expected to narrow from 2.6 per cent of GDP in 2015-16 to 0.8 per cent of GDP by 2017-18. A fiscal deficit of 0.4 per cent of GDP is expected in the PNFC sector for 2015-16, contributing to an NFPS deficit of 3.2 per cent of GDP in 2015-16.

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

The cash balance of the Commonwealth general government sector is expected to remain in deficit over the forward estimates, with a deficit of 2.1 per cent of GDP in 2015-16 improving to a deficit of 0.8 per cent of GDP in 2017-18. At the state level, the expected 2015-16 deficit of 0.2 per cent of GDP will become broadly balanced in 2017-18.

As shown in Chart 4.3, the consolidated general government sector cash balance is expected to be a deficit of 2.7 per cent of GDP in 2015-16, before improving to a deficit of 1.1 per cent of GDP in 2017-18. A cash deficit of 0.4 per cent of GDP is also expected in the PNFC sector in 2015-16, contributing to an NFPS deficit of 3.1 per cent of GDP in 2015-16.

Chart 4.3: Consolidated cash balance by sector[(a)]



(a) Data for the PNFC sector (and therefore the NFPS) are not available beyond 2015-16.

NET DEBT

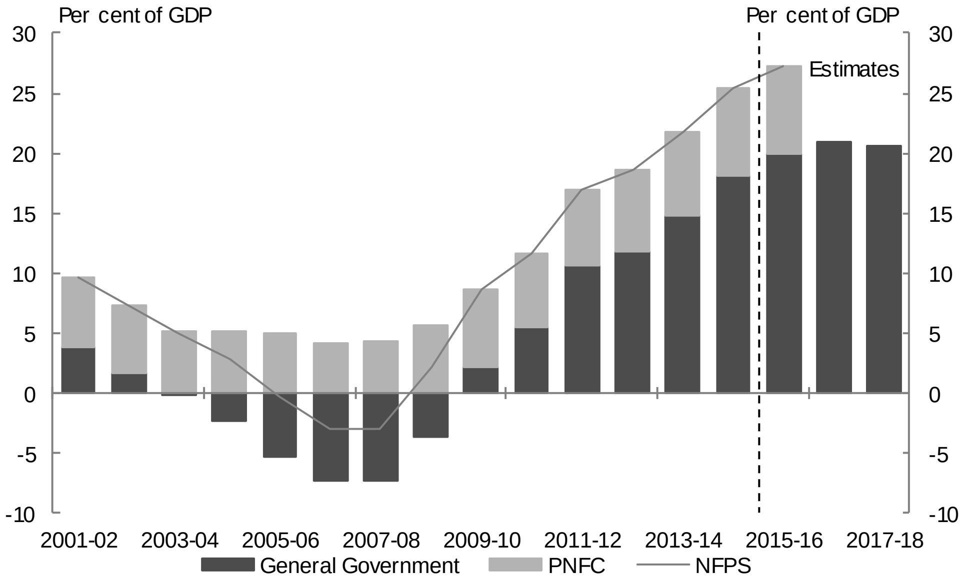
Net debt is the sum of selected financial liabilities (deposits held, advances received, government securities, loans and other borrowing) less the sum of selected financial assets (cash and deposits, advances paid, investments, loans and placements). Net debt does not include superannuation-related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

As shown in Chart 4.4, consolidated general government sector net debt is expected to increase from 19.9 per cent of GDP in 2015-16 to 21.0 per cent in 2016-17 before declining to 20.6 per cent of GDP in 2017-18.

Commonwealth general government sector net debt as a proportion of GDP is expected to increase from 17.3 per cent in 2015-16 to 18.0 per cent in 2016-17 before declining to 17.6 per cent of GDP in 2017-18. State net debt as a proportion of GDP is expected to peak at 3.4 per cent in 2016-17, before declining to 3.1 per cent of GDP in 2017-18. The local government sector is expected to continue to have negative net debt, that is, selected financial assets will exceed selected financial liabilities.

Commonwealth net debt is expected to continue to make up the bulk of consolidated net debt.

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



(a) Data for the PNFC sector (and therefore the NFPS) are not available beyond 2015-16.

THE AUSTRALIAN LOAN COUNCIL

The Australian Loan Council (Loan Council) is a Commonwealth-state council that coordinates public sector borrowing. It 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 in 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.

Outcome of the 2015 Loan Council meeting

The Loan Council met on 9 April 2015 to consider Loan Council Allocation nominations for 2015-16. The Loan Council approved each jurisdiction's nominated allocation. In aggregate, the nominations represent a deficit of $49.5 billion (Table 4.1). The states nominated a deficit of $4.2 billion and the Commonwealth nominated a deficit of $45.4 billion.

Developments since the 2015 Loan Council meeting

As part of the Loan Council arrangements, all jurisdictions are required to update their Loan Council Allocation to reflect their budget and to provide an explanation to the Loan Council if they are likely to exceed the tolerance limit.

2015-16 Loan Council Allocation budget updates will be available in the states' 2015-16 budgets.

The Commonwealth's 2015-16 Loan Council Allocation budget update is available in Budget Paper No. 1, *Budget Strategy and Outlook 2015-16, Statement 9: Budget Financial Statements, Appendix B*.

Table 4.1: Loan Council Allocation nominations for 2015-16[(a)]

	NSW	VIC	QLD	WA	SA	TAS	ACT	NT	C'wlth	Total
	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m
Nominated 2015-16 LCAs										
General government sector cash surplus(-)/deficit(+)	338	-227	-571	1,829	-43	28	486	20	27,714	
PNFC sector cash surplus(-)/deficit(+)	2,672	-5,108	667	642	246	211	123	30	4,484	
NFPS cash surplus(-)/deficit(+)(b)	3,012	-5,433	96	2,471	204	239	602	50	32,198	
plus Acquisitions under finance leases and similar arrangements	46	1,050	195	5	0	0	0	0	2	
equals ABS GFS cash surplus(-)/deficit(+)	3,057	-4,383	290	2,476	204	239	602	50	32,200	
minus Net cash flows from investments in financial assets for policy purposes(c)	-1,234	116	249	0	-3	-2	0	11	-14,217	
plus Memorandum items(d)	1,048	401	422	-628	-548	57	25	0	-1,044	
Loan Council Allocations	**5,339**	**-4,098**	**463**	**1,848**	**-341**	**297**	**627**	**39**	**45,373**	**49,547**
2015-16 tolerance limit(e)	1,689	1,178	1,236	871	365	165	106	131	8,176	

(a) Loan Council Allocation (LCA) nominations for 2015-16 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. Each jurisdiction will publish an updated LCA estimate as part of its budget documentation.

(b) The sum of the general government and PNFC sector balances may not equal the NFPS balance due to inter-sectoral 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 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.

(e) 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 two per cent of NFPS cash receipts from operating activities in each jurisdiction.