6. MANAGING THE STATE'S ASSETS AND LIABILITIES

- The Government is establishing fiscal principles to help support the State's balance sheet, and deliver essential services and infrastructure, while maintaining a strong credit rating.
- This Budget takes a more prudent and responsible approach to managing the State's assets and liabilities, considering more efficient approaches to certain State funds, including the NSW Generations Fund (NGF). Furthermore, the Government is slowing down the rapid growth in gross debt to help take pressure off the State's interest expenses in the current economic and fiscal climate.
- Gross debt is projected to grow to $173.4 billion by June 2026, $14.8 billion lower than the previous projection in the 2023 Pre-election Budget Update. This is primarily driven by a temporary suspension of the contributions into the NGF and the restructuring of the Transport Asset Holding Entity (TAHE).
- Other factors supporting lower gross debt than previously forecast include an updated infrastructure plan and a focus on a return to an operating surplus (aided by the Comprehensive Expenditure Review). Net cash flows from operating activities are projected to return to surplus in 2023-24 and remain in surplus thereafter.
- Net debt is projected to peak at 12.6 per cent of gross state product (GSP) by June 2027. It is estimated to be 12.5 per cent by June 2026, 1.5 per cent below the projection at the 2023 Pre-election Budget Update.
- The State's total assets were $574.3 billion at June 2023 and are projected to grow to $653.6 billion by June 2027. This is one of the benefits of retaining the State's assets for the people of New South Wales.
- Net worth was $326.1 billion at June 2023 and is projected to grow to $347.0 billion by June 2027. This is supported in part by the State's growing asset base.

6.1 Stabilising the State's debt position

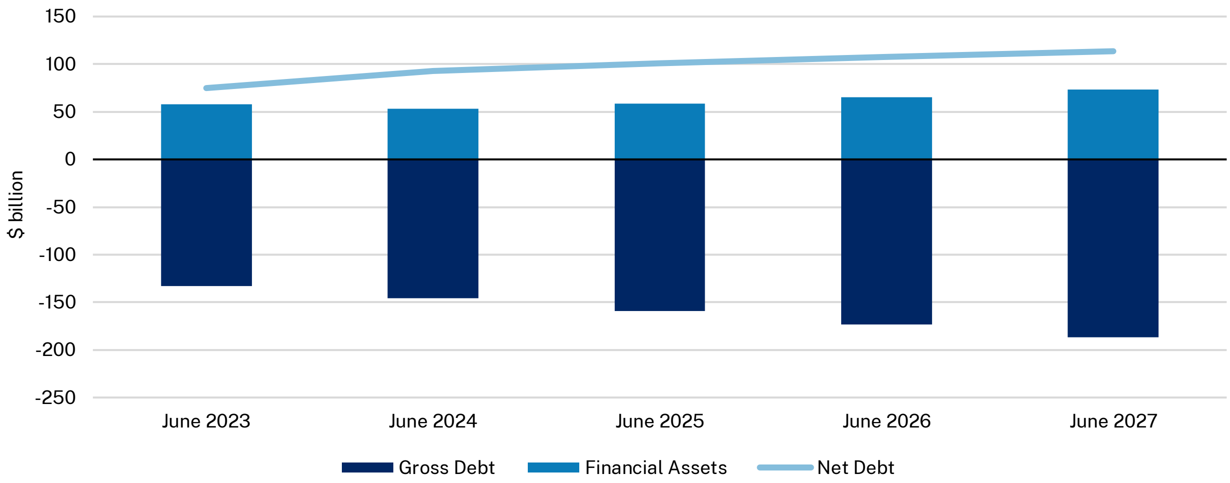
By stabilising its infrastructure plan through initiatives such as the Strategic Infrastructure Review and by letting some of the revenue uplift flow through to the bottom line, this Budget takes the first step towards stabilising the State's net debt below 14.0 per cent of GSP that was projected at the 2023 Pre-election Budget Update.

The Strategic Infrastructure Review led by Ken Kanofski was tasked with identifying infrastructure projects and programs that should no longer proceed or should be delayed or de-scoped, to get the State's infrastructure pipeline back on stable footing.

The Government now projects the State's infrastructure plan will be around 2 per cent of GSP from 2026-27 onwards down from its peak of 3.3 per cent in 2019-20. This will allow the Government to replace its existing asset base in line with depreciation while supporting investment that will help grow the broader economy.

These measures contribute to the forecast for a gross debt of $186.7 billion by June 2027. This is also helping stabilise net debt to GSP around 12.6 per cent by June 2027.

Chart 6.1: General government sector net debt[1], gross debt and financial assets



Financial assets included in net debt

The State's investment funds generate returns that can either be spent or reinvested to support policy aims. The investment funds also support the State's fiscal position and, as financial assets, reduce the State's net debt. It is essential to manage the State's assets prudently and efficiently to ensure opportunities are maximised while risks are minimised.

Financial assets included in the calculation of net debt were $58.0 billion at June 2023, which was $7.7 billion higher than projected at the 2023 Pre-election Budget Update. This is primarily driven by a higher cash balance for payments at June 2023. These assets also include the State's investment funds and other financial assets.

The Government will temporarily suspend contributions to the NGF in 2023-24. Contributions are budgeted to recommence from 2024-25 to 2026-27, while the Government considers further policy decisions, with the NGF's balance projected to grow from $16.0 billion at June 2023 to $39.2 billion by June 2027. The Government will also investigate how certain State funds could be more efficiently managed by TCorp to achieve better risk-adjusted returns.

[1] The estimates of net debt at June 2025 and beyond do not include planned cash receipts of $1.6 billion in 2024-25 from the recycling of the investment for developing the Central West Orana transmission project. This is because the anticipated cash payment will form part of a larger service concession transaction which, in accordance with the budget policy for major asset transactions, will not be recognised until finalised.

Box 6.1: Improving the management of the State's investment funds

Over time, the State has set up various investment funds, each with their own specific legislated purpose. This includes funds such as the Treasury Managed Fund (TMF- the State's self-insurance fund), the NGF, and the NSW Infrastructure Future Fund (NIFF) among others.

Following an inquiry by the NSW Parliament's Standing Committee on State Development, the Government will temporarily suspend contributions in 2023-24 to the NGF, reducing the State's gross debt by $7.7 billion. Contributions are budgeted to recommence from 2024-25 to 2026-27. During this time the Government will determine a more appropriate policy regarding contributions to, and debt retirement payments from, the NGF and also consider a more efficient approach to managing certain State funds, including the NGF.

The NGF balance is now projected to be around $55.0 billion by June 2032, compared to the $94.3 billion projected in the 2022-23 Budget. This financially responsible approach to managing the NGF will significantly reduce the potential impact to the State's finances from investing a larger balance in volatile financial markets.

The 2023-24 Budget also includes an underlying budget result that excludes the NGF's net investment returns to provide a more transparent picture of the State's finances (see Chapter 3 Fiscal Strategy and Outlook, Box 3.1).

The Government will continue exploring options to manage the State's financial assets prudently and efficiently. This will help ensure they remain fit-for-purpose to achieve the Government's policy aims over the long term without creating undue risk for the State's finances and broader balance sheet.

The major investment funds are presented in Table 6.1.

Table 6.1: NSW investment funds returns to 30 June 2023

Fund	Inception Date	Fund Balance $ billion[(a)]	Investment Objective %	FY2022-23 Returns %	Returns Since Inception[(a)] %
NSW Generations Fund	Nov-18	16.0[(b)]	CPI + 4.5[(c)]	8.9	6.4
NSW Infrastructure Future Fund	Dec-16	7.4	CPI + 2.0	4.8	3.8
Social and Affordable Housing Fund	Aug-17	1.6	CPI + 4.0	9.2	6.3
Treasury Managed Fund	Mar-99	14.9	CPI + 3.5	9.6	6.7
Snowy Hydro Legacy Fund	Dec-21	1.6	CPI+1.0	6.0	(2.5)
Long Service Corporation Investment Fund	Nov-13	2.2	AWOTE[(d)]+1.0	6.6	6.2

(a) To 30 June 2023.
(b) This does not include cash set aside for debt retirement.
(c) CPI: Consumer Price Index.
(d) AWOTE: Average Weekly Ordinary Time Earnings (AWOTE), this reflects increases in wage inflation.

Financial assets at fair value are projected to grow to $69.6 billion by June 2027, supported by the growth in the State's investment funds over the budget and forward estimates.

Other financial assets included in the calculation of net debt include cash and cash equivalents. Cash and cash equivalents totalled $6.3 billion at June 2023, $6.1 billion higher than projected in the 2023 Pre-election Budget Update. This high cash balance is to meet the cash payments in July 2023. Cash and cash equivalents will decrease to $263 million by June 2027 in line with the more efficient management of the State's cash balance.[2]

[2] The Government has good access to multiple sources of liquidity, which has allowed it to target a lower general government cash balance than in previous budgets, without any material risk of a funding shortfall. This, in turn results in a lower borrowing requirement for the Budget year, consistent with the Government's objective of lowering the State's gross debt.

Financial liabilities included in net debt

Financial liabilities included in the calculation of net debt were $132.9 billion at June 2023. These liabilities include borrowings (including leases), advances received[3], and deposits held[4].

Borrowings at amortised cost at June 2023 have increased by $3.4 billion since the 2023 Pre-election Budget Update. This increase was primarily driven by a $5.0 billion increase in new borrowings in 2022-23 due to bringing forward funding required in the next financial year. This was one of a number of factors that has reduced the 2023-24 Crown's forecast borrowings from $23.2 billion at the 2023 Pre-election Budget Update to $11.6 billion in this Budget.

Key balance sheet movements since the 2023 Pre-election Budget Update are shown in Table 6.2.

Table 6.2: Key balance sheet aggregates of the general government sector

	June 2022 Actual	June 2023 Est. Actual	June 2024 Budget	June 2025	June 2026 Forward Estimates	June 2027
Total Assets ($m)	510,549	574,325	584,618	604,275	632,355	653,603
Financial Assets ($m)	193,513	210,143	203,046	208,662	225,149	235,824
Non-Financial Assets ($m)	317,036	364,183	381,572	395,613	407,205	417,779
Total Liabilities ($m)	223,828	248,224	264,011	277,843	293,818	306,566
Net Worth ($m)	286,722	326,101	320,606	326,432	338,537	347,037
Net Worth as a per cent of GSP[(a)]	41.1	42.5	40.4	39.7	39.4	38.5
Net Debt ($m)	55,781	74,873	92,624	100,974	107,815	113,571
Net Debt as a per cent of GSP	8.0	9.8	11.7	12.3	12.5	12.6
Gross Debt ($m)	108,352	132,914	145,789	159,510	173,373	186,688
Gross Debt as a per cent of GSP	15.5	17.3	18.4	19.4	20.2	20.7

(a) Gross State Product (GSP) for N*ew South Wales from June 2024 to June 2027 is forecast by NSW Treasury*.

[3] Advances Received are advances and loans made from the Australian Government in funding various approved projects. Advances are loans motivated by government policy rather than liquidity management purposes.

[4] Deposits Held are cash and deposits held at banks and other financial institutions on behalf of entities and individuals external to the State.

Box 6.2: Interest expense affordability and refinancing risk

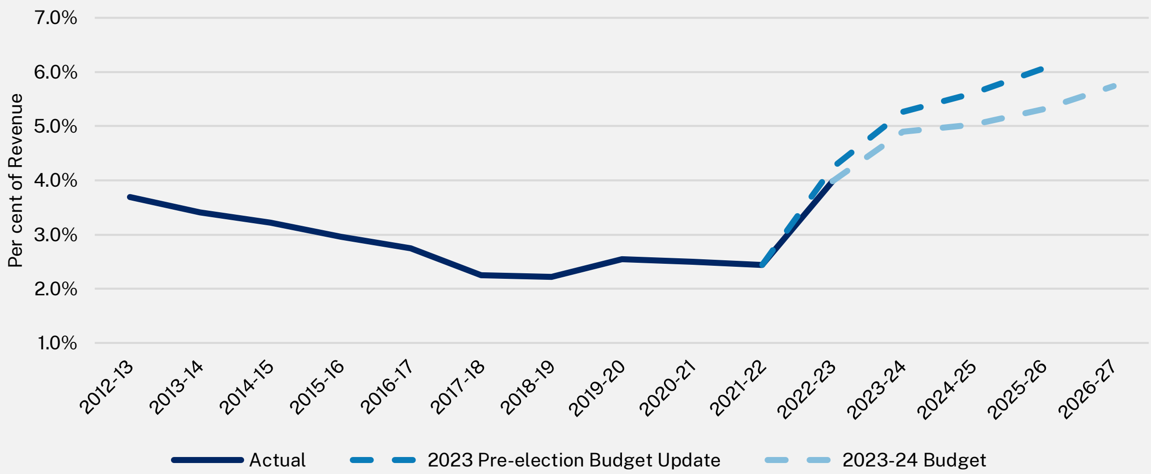
Gross debt is expected to reach $186.7 billion by June 2027 and interest expense is estimated to be $7.0 billion in 2026-27.

Since January 2020, TCorp 10-year bond yields have ranged from a low of around 1.0 per cent (in November 2020) to approximately 4.7 per cent on 1 September 2023. This is primarily due to the rapid change in monetary policy with the RBA raising its cash rate 12 times since May 2022. The cash rate is currently at 4.1 per cent in September 2023.

The weighted average yield of the Crown debt portfolio rose from 2.1 per cent at 30 June 2022 to 2.9 per cent at 30 June 2023. This was driven by new borrowings and refinancing of existing debt at higher interest rates. The weighted average yield of the portfolio is forecast to continue rising over the forward estimates period.

The Government's interest expense as a percentage of revenue is estimated to be 5.3 per cent in 2025-26. This is below 6.1 per cent projected at the 2023 Pre-election Budget Update (see Chart 6.2). Nevertheless, interest expenses continue to place significant pressure on the Government's operating position.

Chart 6.2: Interest expense to revenue - 2023 Pre-election Budget Update vs 2023-24 Budget

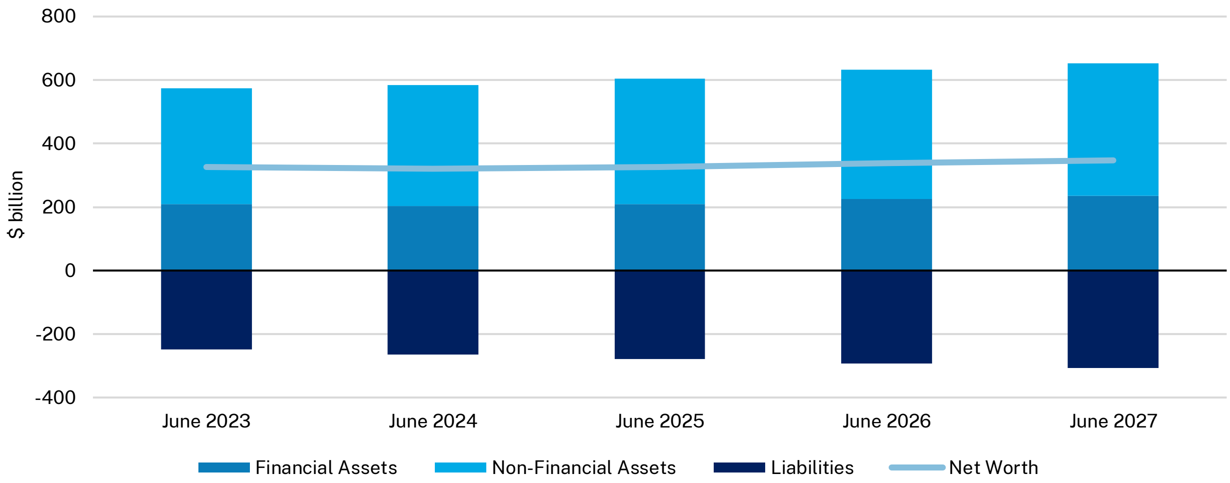


6.2 Net worth continues to grow

General government sector net worth was $326.1 billion at June 2023, $47.5 billion higher than the projection in the 2023 Pre-election Budget Update. This is mostly driven by an upward revaluation of the State's non-financial assets and a better-than-expected operating position in 2022-23.

From June 2023 to June 2027, net worth is estimated to increase by $20.9 billion to $347.0 billion (see Chart 6.3). This increase is driven primarily by a forecast return to budget surpluses from 2024-25, an increase in the value of the equity investments in other public sector entities and the growth of the State's non-financial assets. This is strengthened by the Government's prudent management of its balance sheet, without privatisation of public assets.

Chart 6.3: General government sector net worth to increase over the next four years

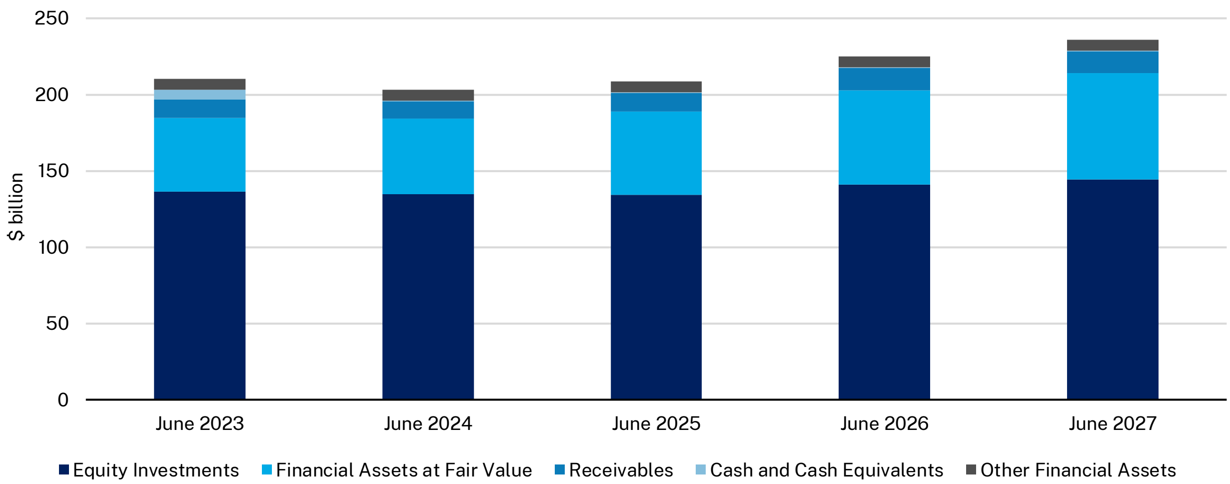


Financial assets included in net worth

The State's total financial assets were $210.1 billion at June 2023[5], $21.6 billion higher than the projection in the 2023 Pre-election Budget Update. This is mainly driven by a $11.5 billion increase in equity investments in other public sector entities due to mostly asset revaluation.

Financial assets are forecast to reach $235.8 billion by June 2027 (see Chart 6.4), driven by the growth in the State's investment funds.

Chart 6.4: General government sector financial assets increasing over time



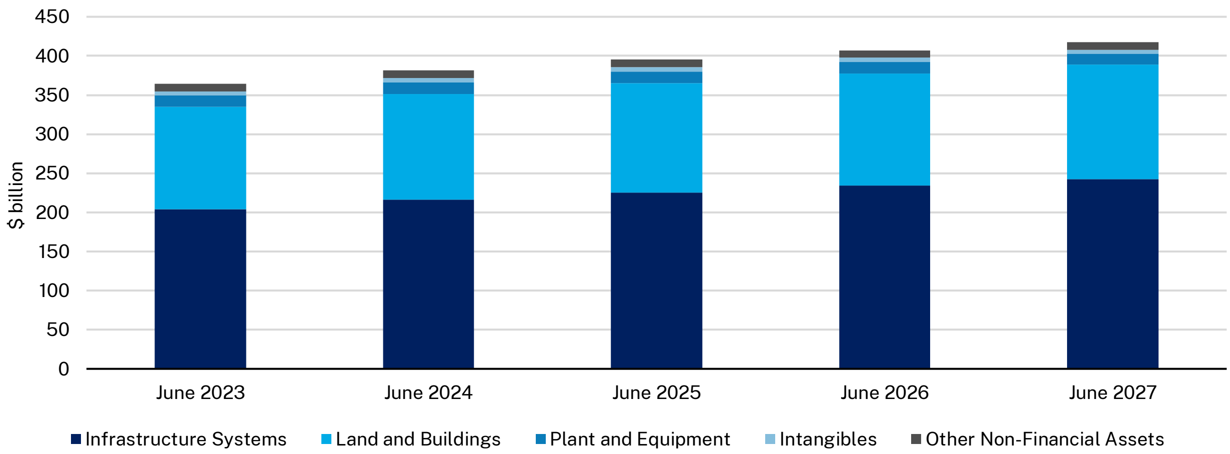
[5] The general government's investments in other public sector entities include the carrying amount of net assets of the Transport Asset Holding Entity (TAHE). The carrying amount of TAHE's net assets, as at 30 June 2023, includes property, plant and equipment measured using an income approach in accordance with *TPP21-09 Valuation of Physical Non-Current Assets at Fair Value* and *AASB 13 Fair Value Measurement*. As a result of the Government's ongoing review of TAHE's future operating model, it is likely that there will be a change in the valuation approach from the income approach to current replacement cost (CRC) during 2023-24. A change in valuation approach to CRC is likely to lead to a materially higher fair value of TAHE's property, plant and equipment that will be reflected in the future Budget estimates.

Non-financial assets included in net worth

The State's non-financial assets were $364.2 billion at June 2023 ($29.0 billion higher than the 2023 Pre-election Budget Update due to upwards revaluations to land and buildings and infrastructure systems). Non-financial assets are estimated to grow to $417.8 billion by June 2027 (see Chart 6.5). This expected increase to June 2027 is primarily due to:

- a projected increase in the State's productive infrastructure systems of $38.4 billion from June 2023 to June 2027, driven by investment in public transport infrastructure
- a projected increase in the value of land and buildings, of $16.2 billion from June 2023 to June 2027, driven by investment in transport, schools, and hospitals.

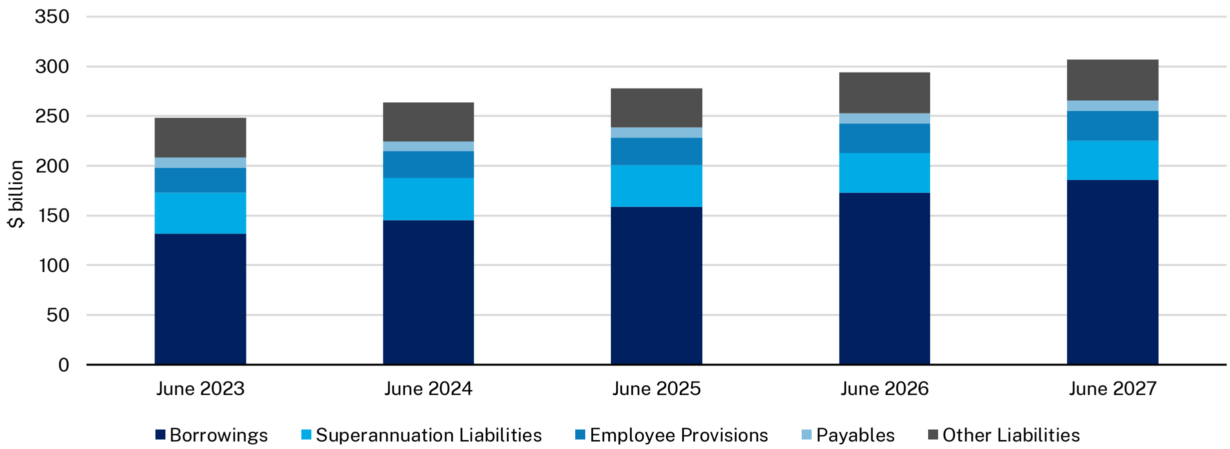
Chart 6.5: General government sector non-financial assets growing over time due to infrastructure investment and asset revaluation



Liabilities included in net worth

Total liabilities were $248.2 billion at June 2023 and are projected to increase to $306.6 billion by June 2027 (see Chart 6.6). This is predominately driven by the State's increased borrowings to fund the investment in infrastructure.

Chart 6.6: Liabilities to increase over the forward estimates



Borrowings represent the largest liability category on the general government sector balance sheet. They are projected to increase over the forward estimates from $132.1 billion at June 2023 to $186.0 billion by June 2027.

TCorp is the State's central borrowing authority and seeks to mitigate financing risk through diversification of funding sources and funding types. This includes the issuance of Green and Sustainability bonds through the NSW Sustainability Bond Programme, lengthening the maturity profile and issuing different types of fixed interest instruments to appeal to a broader set of investors.

The second largest liability of the Government is its defined benefit superannuation liability[6]. The liability was valued at $40.1 billion at June 2023 and is expected to decrease to $39.2 billion by June 2027. In this Budget, the Government has adopted a revised contribution profile, which is $1.7 billion higher over the four years to 2026-27 than the previous schedule. As a result, Treasury's actuaries project that the Government is on track to fully fund its superannuation liabilities by 2040.

Employee provisions, including long service leave, are projected to increase over the forward estimates from $25.4 billion at June 2023 to $30.4 billion by June 2027.

6.3 Managing the State's cash flows

The cash flow statement reports two fiscal measures, which are the net increase in cash held and cash surplus/(deficit). The net increase in cash held is the sum of net cash flows from all operating, investing, and financing activities. Cash surplus/(deficit) comprises net cash from operating activities, plus sales and less purchases of non-financial assets.

This Budget projects a return to a net operating cash surplus in 2023-24, estimated to be $102 million. This indicates that the Government will not borrow to fund its operations. This cash operating surplus is projected to increase to $9.6 billion in 2025-26, which is $1.8 billion higher than the projection in the 2023 Pre-election Budget Update. This is primarily driven by more prudent management of revenues (e.g., coal royalties) by allowing some of the revenue uplift to flow through to the State's bottom line, partially offset by the increase in Government's contribution profile for the defined superannuation liability.

As the State continues to invest in infrastructure such as the Sydney Metro projects, this results in net cash outflows from investments in non-financial assets. These are estimated to be a net cash outflow of $17.0 billion in 2023-24 and a total of $72.0 billion over the four years to 2026-27.

Net cash flows from investments in financial assets for policy purposes represents net cash flows from disposal or return of equity. This includes net equity injections into other public sector entities. In this Budget, this investment is estimated to be $170 million net cash outflows in 2023-24, compared to $2.3 billion net cash outflows projected in the 2023 Pre-election Budget Update. Previously, payments to TAHE were included in net cash flows from investments in financial assets for policy purposes. These payments have been reclassified to cash payments from operating activities in line with the accounting standard.

Net cash flows from investments in financial assets for liquidity purposes include the contributions into and withdrawal from the State's investment funds, such as the NGF and NIFF. In 2023-24, payment for purchases of investments is $7.0 billion lower than projected in the 2023 Pre-election Budget Update. This was led by the Government's decision to temporarily suspend contributions into the NGF in 2023-24, with contributions budgeted from 2024-25 to 2026-27.

[6] The superannuation liability can be measured using two Australian Accounting Standards Board (AASB): *AASB119 Employee Benefits* and *AASB1056 Superannuation Entities*. The superannuation liability reported on the State's balance sheet is the unfunded component of the liability and is governed by AASB119. It should be noted that this Accounting Standard creates a larger and more volatile liability than under AASB1056 due to the use of a conservative valuation discount rate. AASB1056 is the basis used when assessing the Government's funding position. The defined benefit superannuation liability has increased over the last year due to the high inflation experienced, given that pensions are linked to consumer price index (producing a net liability of $19.8 billion as of 30 June 2023 under this basis).

The general government sector cash deficit is estimated to be $43.3 billion over the four years to 2026-27. It reflects the Government's investment in its infrastructure. This cash deficit has to be largely funded by new borrowings, which is the main driver of the increase in gross debt. The cash deficit has improved slightly since the 2023 Pre-election Budget Update.

Chart 6.7: General government sector cash surplus/(deficits)