3. FISCAL STRATEGY AND OUTLOOK

- The 2019-20 Budget continues the Government's track record of responsible financial management.
- Across the four years to 2022-23, the 2019-20 Budget is projecting average budget surpluses of $1.7 billion.
- This strong fiscal position enables the Government to deliver its election commitments alongside a general government infrastructure program of $71.7 billion across the budget and forward estimates.
- The investment in services and infrastructure will have long term economic benefits whilst also meeting the needs of a growing population.
- This budget continues efforts to moderate expense growth to align with revenue growth, with measures to reduce expenditure that leverage recent machinery of government changes.
- The Budget's strong fiscal position has been achieved without raising taxes. This has enabled the Government to reinvest in communities and help families with the cost of living.
- For the fourth consecutive year, New South Wales is projected to end the financial year with negative net debt – projected to be negative $8.8 billion at 30 June 2019.
- The State's strong fiscal position reflects the Government's ongoing commitment to deliver the investment that communities need while keeping debt sustainable and maintaining a triple-A credit rating.

3.1 Strong fiscal discipline today, delivering for tomorrow

This Budget demonstrates the Government's ongoing commitment to responsible financial management. At the same time, New South Wales is investing in services and infrastructure which has only been made possible by:

- maintaining surpluses, without unnecessarily raising taxes
- funding capital expenditure through budget surpluses and asset recycling proceeds as much as possible
- maintaining sustainable debt levels consistent with a triple-A credit rating (see Box 3.1), and
- growing the NSW Generations Fund (NGF), the State's dedicated debt retirement fund.

The *Fiscal Responsibility Act 2012* (FRA) provides a fiscal anchor for the Government with the legislated requirement to maintain a triple-A credit rating. New South Wales is the only jurisdiction to legislate this requirement, making it unique amongst Australian and international jurisdictions. The FRA includes legislated fiscal targets and principles of sound financial management to support the triple-A objective[1] (see Table 3.1 and Appendix E).

The Government believes maintaining the State's triple-A credit rating is important during uncertain economic times. Not only does it keep interest costs for the State as low as possible, it is a signal of fiscal discipline and economic strength. Yield spreads between triple-A and lower-rated government bonds can widen significantly during periods of economic stress, leading to higher costs of borrowing for non-triple-A rated governments. Additionally, a triple-A rating allows the State to maintain access to wholesale funding markets during times of market stress.

Table 3.1: Fiscal objective and targets

Requirements of the *Fiscal Responsibility Act 2012*	Target met?	Explanation
Objective: Maintain the triple-A credit rating		
S&P Global	✓	Reaffirmed AAA with a stable outlook in September 2018
Moody's	✓	Reaffirmed Aaa with a stable outlook in September 2018
Target 1: Annual expense growth less than the long-term average revenue growth	✓	Annual expense growth is less than long-term average revenue growth (5.6 per cent) across all five years
Target 2: Elimination of the State's unfunded superannuation liability by 2030	✓	NSW is on track to fully fund its superannuation liabilities by 2030 as per the triennial review completed in October 2018

The State's dedicated $10.8 billion debt retirement fund, the NGF, further supports the State's triple-A credit rating, allowing debt to be maintained at sustainable levels over the long term – see section 1.4 in Chapter 1 for more details.

Box 3.1: New South Wales is part of the world-class triple-A club

Both major global credit rating agencies, Moody's and S&P Global, re-affirmed the State's triple-A credit rating in September 2018. Once again New South Wales has been determined to have the lowest possible risk of defaulting on its debt – synonymous with very strong fiscal and economic health.

New South Wales is one of only two Australian states (see Chart 3.1) and one of five international sub-sovereigns rated triple-A by both major credit rating agencies[2].

A triple-A credit rating reflects an independent assessment of a strong fiscal and economic position, a solid institutional and governance framework, and sustainable debt levels. Triple-A rated jurisdictions are generally able to borrow at lower interest rates given their strength and stability relative to lower-rated governments.

[1] The principles of sound financial management are: responsible and sustainable spending, taxation and infrastructure investment; effective financial management, including sound policies and processes; and achieving intergenerational equity.

[2] This excludes the United States where states are assessed under a different methodology.

Chart 3.1: Credit ratings of Australian States and Territories as at June 2019

3.2 Fiscal discipline is the cornerstone of New South Wales' Budget

Due to tightening economic and revenue conditions, the Government has maintained a strong focus on expense discipline.

A budget surplus of $802 million is expected in 2018-19. The Government is projecting to deliver surpluses across the four years to 2022-23 (see Table 3.2) which average $1.7 billion per year.

Maintaining budget surpluses is important as this helps fund infrastructure (keeping debt at sustainable levels) and provides a buffer in times of economic uncertainty to allow the Government to respond to fiscal shocks or other unforeseen events (e.g. drought).

Table 3.2: General government sector budget result aggregates

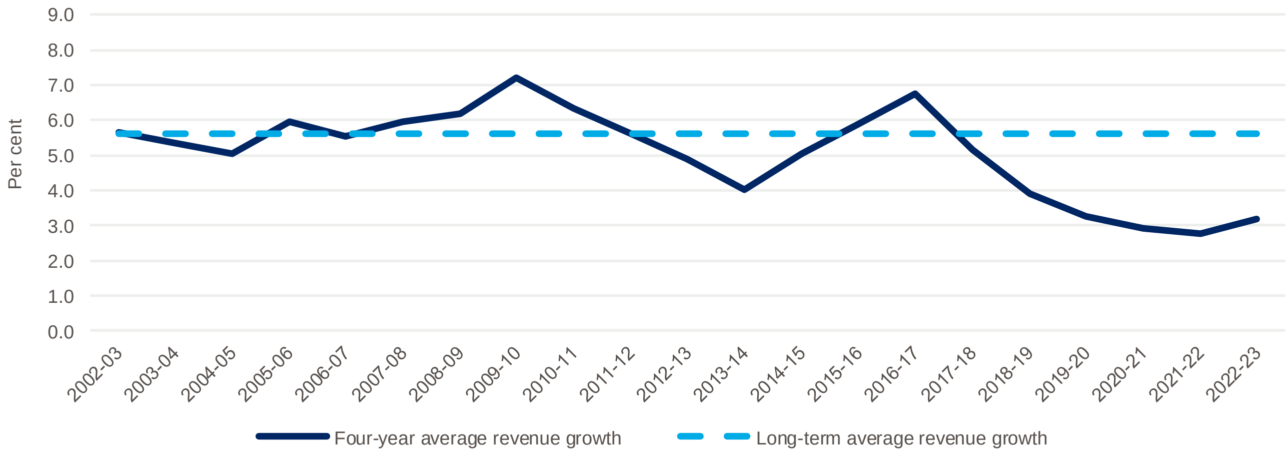
	2018-19 Revised	2019-20 Budget	2020-21	2021-22 Forward Estimates	2022-23
Revenue ($m)	81,128	84,316	87,632	90,018	92,009
Revenue growth (per cent p.a.)	0.6	3.9	3.9	2.7	2.2
Expenses ($m)	80,326	83,300	86,405	88,016	89,410
Expense growth (per cent p.a.)	5.0	3.7	3.7	1.9	1.6
Budget Result ($m)	802	1,016	1,227	2,002	2,599
Per cent of GSP	0.1	0.2	0.2	0.3	0.3

A solid revenue base with emerging pressures

The State's revenue position remains strong. However, revisions to stamp duty and GST revenue have put pressure on revenue growth, with marginally lower revenue in 2018-19 than previously forecast.

Revenue growth is forecast to average 2.8 per cent over the four years to 2021-22 (see Chart 3.2), which is higher than the 2.7 per cent forecast at the 2019 Pre-election Budget Update. This is primarily due to an increase in sales of goods and services, and revised returns on financial asset investments. Further detail on revenue can be found in Chapter 4.

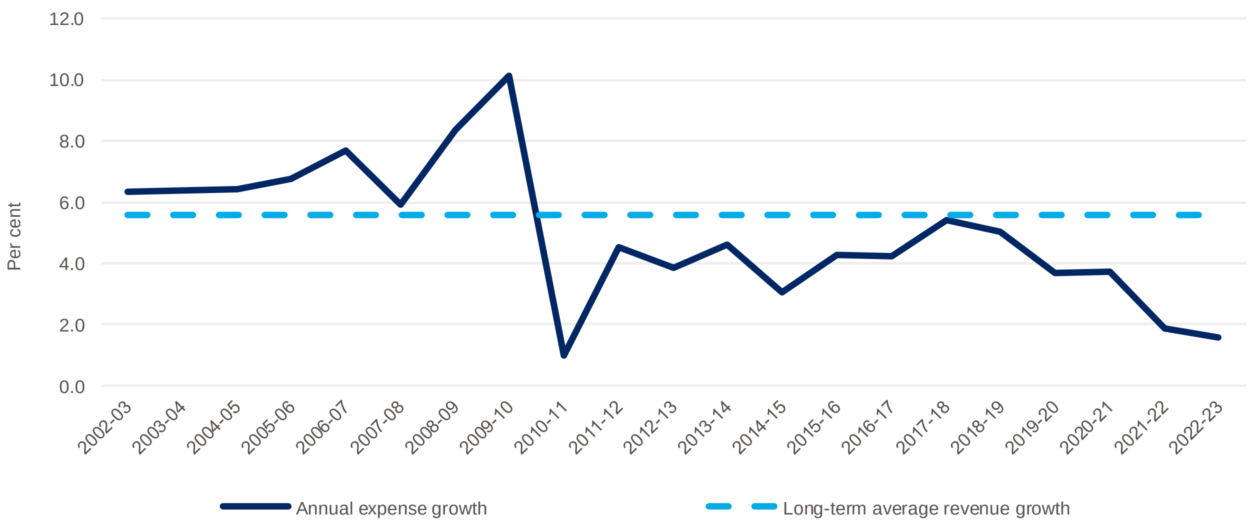
Chart 3.2: Four-year average revenue growth compared to long-term revenue growth



Maintaining tight control of expenses

In 2019-20, the annual expense growth rate is projected to be 3.7 per cent, which is below the long-term average rate of revenue growth (5.6 per cent) as required by the FRA (see Chart 3.3). As revenue growth continues to diverge further from the long-term rate, the importance of maintaining tight control on expenses grows. The Government's disciplined approach to financial management and continued achievement of its FRA targets are helping manage expenses.

Chart 3.3: Annual expense growth



Expense growth is expected to be 5.0 per cent in 2018-19, in line with the projection at the 2019 Pre-election Budget Update. This result has been achieved despite increased expenses flowing from the latest revaluation of NSW Self Insurance Corporation's (SICorp) scheme liabilities. This has been partially offset by a more efficient use of existing resources, providing more streamlined service delivery and reflecting recent machinery of government changes.

Changes in the budget result since 2018-19 Budget

Since the 2018-19 Budget and 2019 Pre-election Budget Update there have been a number of movements in expenses and revenue that have impacted the budget result.

The projected budget surpluses in the near term to 2020-21 have been revised down since the 2019 Pre-election Budget Update, primarily due to a write-down in Commonwealth GST receipts, lower transfer duty forecasts and reduced revenue from fines (see Table 4.3 in Chapter 4).

Table 3.3: Reconciliation of 2019-20 Budget to 2018-19 Budget(a)

	2018-19 Revised	2019-20 Budget	2020-21 Forward Estimates	2021-22
	$m	$m	$m	$m
Budget result: 2018-19 Budget	**1,425**	**1,528**	**1,412**	**1,855**
Changes from 2018-19 Budget to 2019 Pre-election Budget Update				
Policy measures				
Revenues	(79)	572	871	335
Expenses	(454)	(688)	(919)	(802)
Total policy measures	**(533)**	**(116)**	**(48)**	**(467)**
Parameter and other budget variations				
Revenues	264	175	509	587
Expenses	(310)	(443)	(424)	(357)
Total of parameter and other budget variations	**(46)**	**(268)**	**85**	**230**
Total policy measures, parameter and other budget variations	**(579)**	**(384)**	**37**	**(237)**
Budget result: 2019 Pre-election Budget Update	**846**	**1,143**	**1,449**	**1,617**
Changes from 2019 Pre-election Budget Update to 2019-20 Budget				
Policy measures				
Revenues	...	263	830	590
Expenses	11	(452)	(207)	202
Total policy measures	**11**	**(188)**	**623**	**792**
Parameter and other budget variations				
Revenues	(138)	(402)	(306)	(162)
Expenses	83	464	(538)	(244)
Total of parameter and other budget variations	**(55)**	**61**	**(845)**	**(406)**
Total policy measures, parameter and other budget variations	**(44)**	**(127)**	**(221)**	**386**
Budget result: 2019-20 Budget	**802**	**1,016**	**1,227**	**2,002**

(a) Positive amounts reflect a positive impact on the budget result e.g. an increase in revenue or a decrease in expenses.

NSW infrastructure program delivers for the next decade

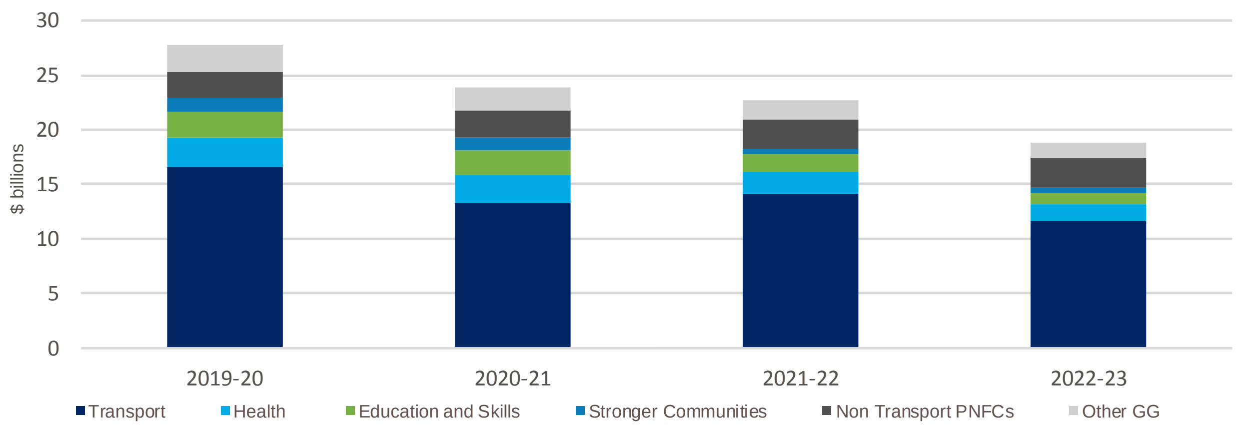
The 2019-20 Budget delivers another record general government infrastructure program with $71.7 billion projected over the four years to 2022-23. This represents an increase of $6.0 billion over the comparable four-year total at the 2018-19 Budget, driven by an additional $3.2 billion for Sydney Metro West, an additional $1.2 billion for the More Trains More Services program, and $1.6 billion more on hospitals and other infrastructure investments.

The Government is committed to investing in the economy and building for tomorrow, with future expenditure in productive infrastructure, including:

- metro projects such as Sydney Metro West, Sydney Metro City and Southwest, and North South Metro Rail Link
- new and upgraded roads including Pacific Highway, Princes Highway and Sydney Gateway
- investments in health for the new Bankstown-Lidcombe Hospital and redevelopment of the Royal Prince Alfred Hospital
- additional investment in education with eight new and 32 upgraded schools.

For the non-financial public sector (NFPS), over the next four years capital expenditure is projected to reach $93.0 billion, with road, rail and other transport infrastructure accounting for 60 per cent. The Government is also investing in other priority areas with health, education and justice related infrastructure making up 21 per cent of the four-year total (see Chart 3.4 and Budget Paper No. 2 *Infrastructure Statement*).

Chart 3.4: Non-financial public sector capital expenditure by cluster[a][b]



(a) Clusters are reported where appropriate to align with new machinery of government changes announced in April 2019, which take effect from 1 July 2019.
(b) Numbers represented in the chart are on an eliminated government sector basis. This chart does not agree with individual agencies reporting which is done on an uneliminated basis, predominately due to showing the impact of leases provided by other clusters.

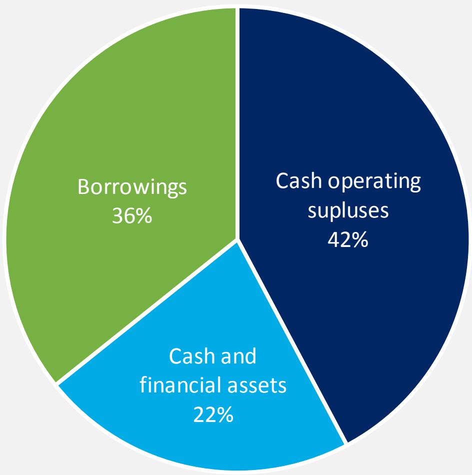
The Government is funding the State's record infrastructure program while maintaining debt levels consistent with a triple-A credit rating. This has been made possible by funding capital expenditure through consistent budget surpluses, reinvesting asset recycling proceeds, and maintaining manageable borrowing levels (see Box 3.2).

Box 3.2: Managing the Budget in times of uncertainty

Maintaining strong fiscal discipline and manageable levels of debt helps to insulate New South Wales against economic shocks. It also provides flexibility for the Government to respond in times of need such as the 2018-19 Emergency Drought Relief Package, as New South Wales is experiencing one of its driest years on record.

The Government's strategy for funding its record infrastructure program ensures that the State maintains acceptable levels of debt consistent with a triple-A rating (see Chart 3.5). Over the five years to June 2023, almost two-thirds of general government sector capital expenditure will be funded from non-debt funding sources, e.g. annual cash operating surpluses and the State's cash and financial asset investments (predominantly the proceeds of asset recycling).

Chart 3.5: Funding of the capital program across five years to June 2023[(a)]



(a) Source: General government sector cash flow statement as published in Appendix A1

NSW to deliver a fourth consecutive year of negative net debt

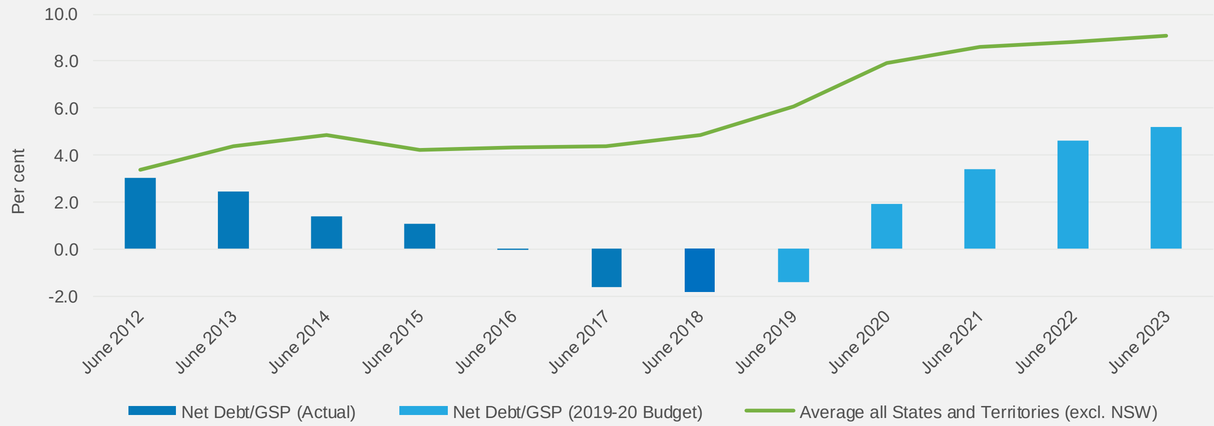
Net debt, which is a measure of the State's capacity to repay its debt immediately, is projected to be negative $8.8 billion at June 2019. This will be the fourth consecutive year of negative net debt, having reached a record low of negative $11.2 billion in June 2018. This negative net debt has been driven by the Government's successful asset recycling program and balance sheet reform, which has meant that over the past four years the Government has been able to minimise its reliance upon borrowings. New South Wales' net debt remains the lowest out of all States and Territories (see Box 3.3).

Box 3.3: New South Wales delivers low net debt relative to other jurisdictions

The Government is maintaining a sustainable level of debt consistent with a triple-A credit rating. The State is expected to deliver a fourth consecutive year of negative net debt with a June 2019 projection of negative 1.4 per cent of gross state product (GSP), lower than the average of all other State and Territories. This is projected to grow to 5.2 per cent of GSP by June 2023, as the State continues its transformative infrastructure investment.

Despite the projected increase in net debt to GSP over the forward estimates, New South Wales will remain well below the average of all other States and Territories at 9.1 per cent in June 2023 (see Chart 3.6 below).

Chart 3.6: Net debt to GSP: New South Wales vs other States and Territories[(a)(b)]



(a) Source: most recent published State and Territory budget data.
(b) June 2023 excludes South Australia as latest published data is 2018-19 Mid-Year Budget Review.